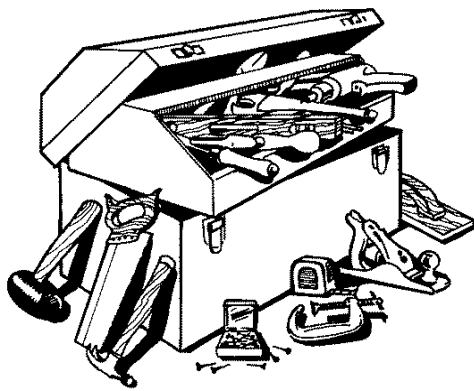


Contract Administrator's Toolbox



***A collection of resources for administering
contracts involving funding from the
Department of Health and Family Services***

Office of Program Review and Audit

2001

Contract Administrator's Toolbox

Foreword

Greetings --

Most of you know the Office of Program Review and Audit (OPRA) as the office within the Department of Health and Family Services that collects and reviews audit reports, and that produces statewide audit and financial management documents, such as the *Financial Management Manual*, the *Provider Agency Audit Guide*, and the *Audit Alert Bulletin*.

OPRA has other responsibilities, as well, including working within the department on a wide range and variety of contracting issues. Some of the projects have been department-wide in nature, such as coordinating efforts to create a department model provider contract and creating a *Contract Administrator's Manual* for department staff. Other projects have been specific to a division, such as working with a division to develop pay-for-performance contract language or create a system for monitoring contract agencies. Given that our office is staffed with several auditors, OPRA also, of course, has audited many provider agencies.

With this wealth and variety of experience, OPRA along the way has created a lot of documents related to contracting that we and other DHFS staff have found to be helpful. We have compiled many of these documents in this "Contractor's Toolbox." Just a couple brief comments on the content of the "Toolbox" are in order. First, because much of the material was developed specifically to handle a situation within DHFS, we recognize that not all documents may not fit perfectly the circumstances faced by other purchasers. However, most human services contracting issues are shared by a wide variety of agencies receiving DHFS funds, so we think that most portions of these documents will be relevant to other purchasers.

Second, our goal to describe some best practices that we hope will encourage people on to think of new and better ways to perform contracting work. This material is not intended to be a collection of compliance requirements that everyone must do in all instances. We all are striving to find a better way to perform a tough job, and we suspect you are, too.

We hope you find the enclosed material to be helpful, too. If you have any questions or comments about the "Toolbox," please feel free to contact us at (608) 266-2924. My e-mail address is coopepw@dhfs.state.wi.us.

Good luck in tackling the many unexpected challenges the world of contracting will inevitably toss your way!

Patrick Cooper, Director
Office of Program Review and Audit

Introduction

This “Contract Administrator’s Toolbox” was created as a resource for state, county, and other managers and staff who have responsibility for developing, administering, and monitoring contracts for services. The focus is on contracts involving funding from the Department of Health and Family Services (DHFS), but we believe the contract administration tips and best practice suggestions offered in the “Toolbox” are broadly applicable to the administration of contracts generally.

The “Toolbox” was created initially as a supplement to a two-hour training session on contract administration held in April 2001. We believe the document’s content is self-explanatory and valuable to readers even if they did not attend the training. However, to assist in better understanding the context of the “Toolbox’s” content, we have included this brief “Introduction” to the “Toolbox,” that was not included in the original version of the document.

Chapter 1 of the “Toolbox” provides a brief high-level description of the five basic steps in the procurement process. We viewed breaking down the overall process into discreet steps as necessary in order to focus training and related materials on high priority topics.

The first step of the procurement process is planning the purchase of services. A key step the purchaser needs to take in the planning phase is clearly defining the standards of performance the purchaser needs the provider to achieve as a condition of payment. Chapter 2 presents some important qualities of good measures of effective performance that the purchaser may want to consider when developing standards and contract deliverables. Chapter 3 offers some thoughts and ideas on how purchasers may want to pursue the growing interest in developing outcome-based and pay-for-performance contracts.

The second overall step in the procurement process is soliciting providers. Complying with key procurement requirements is something all purchasers need to consider. Chapter 4 includes excerpts from the DHFS *Allowable Cost Policy Manual* on procurement requirements that need to be met in order to ensure that contractor payments are allowable charges to programs receiving DHFS funds. Chapter 5 is a re-print of audit guidance in the *State Single Audit Guidelines* that highlights instructions auditors are to follow when doing audits counties and other governmental entities. Included in the guidelines is the auditors’ responsibility to check to see that the purchaser (mostly counties, when it comes to DHFS funds) followed procurement requirements when administering DHFS funds.

Step three of the overall procurement process is writing the contract. Making certain the contract includes all required items to protect the purchaser’s interests is important to do. Chapter 6 includes a checklist OPRA created for double-checking contracts it had been asked to review, which others may find useful. One of the most important components of a contract is, of course, the payment language. Chapter 7 is a discussion of both the basic types of methods of payment that a purchaser can use, and the pros and cons of each of the various

payment methods.

Another important financial management decision that needs to be made by a purchaser when developing a contract is whether to include a requirement that a purchaser needs to submit an annual audit and, if so, what type of audit. Making this decision is more complicated than it may seem, because making the right decision invariably requires the purchasers to think carefully about the nature and magnitude of risks the purchaser faces in doing business with a potential provider. Chapter 8 of the “Toolbox” re-prints risk assessment strategies and tools that were originally included in the DHFS *Provider Agency Audit Guide*. As highlighted in this chapter, a key step in making a decision on whether to require an audit is the purchaser making a decision on the scope of contract monitoring that purchaser staff will perform.

This leads to step four of the overall procurement process, which is monitoring the performance of the provider, once the contract has been signed. The “Toolbox” has several chapters dedicated to this phase of the procurement process:

- ✓ Chapter 9 includes a sample site review tool that contract administration staff for a purchaser may find helpful when conducting site visits of a provider.
- ✓ Chapter 10 is extended excerpts from the DHFS *Contract Administrator’s Manual* that addresses a wide variety of contract monitoring and other duties related to administering on-going contracts.
- ✓ Chapter 11 is brief but includes what we believe are important “words of wisdom” from experienced contract administrators on tips for effectively managing contracts, including reading key “red flags” that a provider’s performance may be deteriorating.
- ✓ Chapter 12 discusses the options available to a purchaser for responding to information that a provider’s performance is not meeting expectations, and the considerations the purchaser may want to make in deciding what actions steps to take.

In the fifth and final phase of the overall procurement process, the purchaser uses the results of monitoring efforts to make a reasoned judgement as to whether or not to re-contract with a provider and, if so, whether the terms of the contract need to change. In Chapter 13, we discuss the considerations that may need to be made in making the difficult decision to cancel or non-renew a contract.

Table of Contents

If viewing in Word, click on the page number for a section to jump to that section.

Page Number

<i>Foreword</i>	<i>i</i>
<i>Introduction</i>	<i>ii</i>
<i>Table of Contents.....</i>	<i>iv</i>
<i>1 Five steps in procurement</i>	<i>1</i>
<i>2 Qualities of effective performance standards</i>	<i>2</i>
<i>3 Buying “outcomes”.....</i>	<i>4</i>
<i>4 Procurement and sub-contracting requirements.....</i>	<i>8</i>
<i>5 Purchase of services audit guidelines.....</i>	<i>10</i>
<i>6 Contract review checklist</i>	<i>14</i>
<i>7 Payment mechanisms.....</i>	<i>17</i>
<i>8 Identifying and assessing risks.....</i>	<i>27</i>
<i>9 Site visit tool for monitoring subgrantee performance</i>	<i>40</i>
<i>10 Monitoring performance, renewing or closing out contracts, and audits</i>	<i>44</i>
<i>11 Words of wisdom from contract administrators</i>	<i>66</i>
<i>12 Action steps</i>	<i>68</i>
<i>13 Canceling or non-renewing contracts.....</i>	<i>71</i>

Contract Administrator's Toolbox

1 Five steps in procurement

For the purposes of this training, we have divided the overall procurement process into five discrete steps. In our view, a purchaser needs to effectively perform these five steps if the purchaser is to achieve procurement objectives and get good value for the purchaser's limited services dollar.

What are the five steps, and what needs to be done? In short, we believe a purchaser needs to:

1. ***Plan the purchase of services*** – Through careful planning clearly demonstrate the need for the services being procured, the results that the purchased service is to accomplish, and the value and linkage of the services to the overall human service delivery network.
2. ***Solicit providers*** - Use open competition where possible and maximize use of accurate, complete, and relevant information on provider capabilities and past performance when selecting a provider to contract with.
3. ***Write the contract*** - Develop effective contracts that communicate expectations, define responsibilities, protect all parties, and help to manage differences. The purchaser needs to specifically define and integrate into the contract the nature and amount of services needed, the standards of quality that must be met, and benchmarks that will be used to judge whether services have met expectations and have delivered the needed results.
4. ***Monitor performance*** - Systematically monitor performance to confirm that the desired results stated in the contract are being achieved. Promote a good working relationship with providers, including offering technical assistance as needed and using multiple opportunities to continuously communicate with providers.
5. ***Use performance results*** - Use documented performance and results in re-contracting decisions, and be willing to make the difficult but necessary decision to significantly change or terminate contracts when poor performance occurs and is unlikely to improve.

If the purchaser effectively performs each of the five steps of the procurement process, the purchaser will have a clearer vision of the overall objectives that its procurements are to achieve. With this vision as a guide, the purchaser will be able to negotiate more effectively from a position of strength based on clear goals, reasonably complete information, and sound strategy.

2 Qualities of effective performance standards

The following list of performance standards was developed as part of a departmental project to focus attention on criteria that performance standards should meet - especially those intended to be used for the purposes of influencing contractor payment.

The first test of whether a measure is appropriate for use in making contractor payments is, of course, whether the measure is directly related to the fundamental goals of the program being funded by the Department. After this test is passed, it then needs to be confirmed that a potential pay-for-performance measure is feasible to actually use. In making this assessment, based on our experience, we have developed seven criteria which we believe could be used to gauge how appropriate and feasible a measure might be for use in making payments.

We realize it may not be possible to find measures that fully satisfy all these criteria. In any event, measures should be judged carefully against these standards in order to confirm that they are feasible and can be readily used in an overall payment scheme.

1. ***Quantifiable.*** The performance information needs to be quantifiable. Under the alternative, in which contractors would submit more qualitative, subjective, information, it would be difficult to ensure both the quality of information submitted and the consistent interpretation of contractor information by the purchaser's staff. There also would likely be continuous disputes over payment decisions made by the purchaser.
2. ***Precise and unambiguous.*** The information related to a performance measure should be precise and essentially speak for itself. Performance measures should be worded so they are not ambiguous, not subject to multiple interpretations, and do not contain unintended incentives which encourage programs to move in unwanted directions.
3. ***Reliable and consistent.*** Procedures for collecting, recording, and reporting the performance information need to be simple, direct, and lend themselves to a minimal likelihood for inconsistent application. In contrast, performance measures that are based on numerous staff statewide applying individual (albeit presumably trained) judgments regarding changes in client conditions, could be open to inter-rater inconsistencies and potential manipulation. Efforts to counteract these measurement distortions can be devised, but these may then violate criteria #5 (low cost) and #6 (routine and administratively simple) below.
4. ***Verifiable and documentable.*** The performance information used for making payment should be supported with credible documentation, which is verifiable. Otherwise, performance information could be readily manipulated, with no means of independently confirming the accuracy of the data presented.

5. ***Low Cost.*** Related to point #6 (routine and administratively simple), the effort to collect performance information cannot itself be too costly for the provider, as this could jeopardize support for and compliance with the performance information collection plan, siphon off money needed for the services, and provoke a debate over who should pay the added administrative costs. On the purchaser's side, contract administrators will be required to verify performance information, and the pay-off in terms of improved program performance and increased accountability should be worth the extra time involved.
6. ***Routine and administratively simple.*** In general, performance information that can be routinely collected through the course of normal business operations is likely to be more accurate, reported in a timely manner, and less costly to obtain. Information that can only be collected through complicated, add-on procedures is more likely to be subject to error, while the Department and the contractors will have to incur more training, oversight, and quality assurance efforts in order to support the information collection and analysis effort.
7. ***Timely.*** Information related to a performance measure needs to be obtained in a timely manner for two reasons. One is contractor concern regarding cash flow. If performance information takes a long time to obtain, and if this delays a portion of payment, contractors will be justifiably concerned that this could adversely affect cash flow needs. Since payments generally need to be made on a monthly basis, it may be wise to have performance measures that focus on data that is readily available at the time payments need to be made.

A second reason for timeliness is the desire for prompt feedback. It is simply the case - as embodied in the axiom "swift justice" - that an agency's (or person's) behavior and performance is mostly likely to be affected if the consequences of poor (or excellent) performance are promptly felt.

3 Buying “outcomes”

A major goal of the Department of Health and Family Services is to make sure that agencies we buy services from are providing the outcomes we need at an affordable price. Why? Many reasons are offered:

- ✓ An “outcome” (which is a measure of the extent to which clients truly benefited from services) is a better way to achieve real accountability, because we will have information on what’s most important to the public – evidence that clients benefited from services provided.
- ✓ Buying outcomes is better than the alternative most in use in the past, which is funding allowable costs irrespective of the degree to which programs benefited clients. Buying outcomes gives the incentives we want.
- ✓ A focus on outcomes can promote efficiencies, loosen regulations, and open up program and administrative options for the provider, as the focus shifts away from how a provider achieves outcomes and on to whether outcomes are achieved.
- ✓ The process of figuring out what outcomes a purchasing (and contract) agency really needs and expects is itself a valuable process, and can only serve to focus communication and help all parties in setting meaningful priorities.

But, while this is a well supported goal that is probably shared by many others as well, we need to be honest with ourselves about how close we are to accomplishing the objective of contracting and paying according to outcomes. A requirement that outcomes be met in a contract – perhaps even going to far as making payments to a provider contingent on delivering the outcomes – is frightening to many. And, there may be valid reasons for this trepidation.

1. **Limited knowledge.** Unless the cause and effect relationships are clear -- i.e. what set of "causes" really produces the outcome effect we want -- providers may be quite nervous about being asked to accept responsibility for achieving outcomes as a condition of payment.
2. **Control and causality issues.** Related to the above point, many positive client outcomes are obtained through a convergence of forces, not all of which may be under the control of the provider. Providers may be asked to take responsibility for something they can't fully control.
3. **Risks.** Because of the these factors, a provider may simply not really know the relationship between the costs to be incurred in trying to produce outcomes and the number of outcomes that will result – as well as the income to be earned in producing these outcomes. This creates a big financial risk for both the provider and the purchaser.

4. **Measurement issues.** Some outcomes are quite difficult to measure and create a host of issues about whether a provider is really capable of isolating the outcomes related to the provider's program efforts.
5. **Administrative costs.** The costs to administer a system to collect and report credible outcome information can be high and divert time and resources away from the program.

All of the above, and more, can create anxiety among potential providers, and can lead to a real concern among purchasing staff, which is that the purchaser may issue a bid that no one responds to. That is, the provider community will see too many risks associated with agreeing to accept payment based on outcomes, and we will find no one to do the work we need to have done.

In short, it does not make sense to adopt an “Outcomes at all cost” posture as it relates to provider contracts, to say that “process goals don’t matter” and all we’re interested in is whether the outcomes are delivered. In too many areas, we are still learning and simply know too little about what it takes to deliver outcomes. Therefore, we need to approach the notion of linking results to contracts with our eyes wide open.

But, having said that, we need to try to lay the groundwork for progress. We first need to recognize that measuring outcomes is different than paying according to outcomes. Paying according to outcomes without first carefully working through important program, data measurement, operational, and financial issues will create unnecessary risks. On the other hand, while paying according to outcomes may be premature in several areas, there really is no reason why we cannot be working on defining and measuring outcomes, and start to collect better information right now on the real results of the programs we fund.

Another step in making progress is recognizing that there is an outcomes measurement hierarchy at work, and that all programs and contracts are at some stage along the hierarchy. We need to be consciously aware of where we are at in this hierarchy, and use this awareness to move ourselves closer to the goal of eventually being in a position to more closely link payments to achieving outcomes. That may take awhile, but the point is we need to make progress.

What is the outcome hierarchy? It goes as follows:

1. **Define Outcomes** – At this stage, program staff are trying to figure out exactly what measurable outcomes they want and need the program to deliver.
2. **Establish data collection system** – At this stage, program staff are evaluating options and deciding on the best, most feasible plan for collecting needed outcome information.
3. **Record outcome information** -- At this stage, providers are collecting the outcome information and finding unexpected issues and glitches in the data system that need to be addressed and resolved.

4. **Report the results** – At this stage, providers begin reporting outcomes to the purchasing agency, and reporting needs and issues are worked out.
5. **Analyze outcome results** – At this stage, the purchasing agency is analyzing the outcome information and deciding how to interpret and evaluate the information, as well as determining what refinements in the information may be needed.
6. **Establish outcome expectations** – At this stage, once data accuracy and interpretation issues are resolved, the purchaser takes the next big step of establishing a threshold of desired or expected performance providers must meet in achieving outcomes.
7. **Establish consequences for exceeding/not meeting outcome expectations** – At this stage, the purchaser establishes and negotiates with providers a set of consequences that could or will be enforced if the expectations are not met. The parties could also consider and agree on a set of positive incentives that accrue to providers if the providers materially exceed performance expectations.
8. **Enforce the consequences** – At this final stage, the purchaser acts to enforce the consequences of failing to meet, or exceeding, performance expectations.

It should be noted that throughout this time period, the purchaser needs to also be collecting timely and reliable provider cost information, so that the purchaser (and provider) can realistically draw a correlation between the production of desirable outcomes and the cost to produce these outcomes.

We would urge top administrators and mid level managers in health and social service agencies at all levels of government (and in non-government agencies) to strive to move along the hierarchy toward better measuring and reinforcing the delivery of desired outcomes. Some steps that could be taken to get there are:

- a. Assess where your agency is at in the above hierarchy – are outcomes for the relevant program(s) identified? Are outcomes being measured, and is the information reliable? Etc.?
- b. Based on your self-assessment of where you at, assess the feasibility and desirability to move up the outcomes hierarchy. If in both instances the answer is “yes” – i.e. it is feasible and desirable -- make a plan to do so.
- c. Make sure that your contract with your provider has two things: (1) clear and unambiguous data collection, retention and reporting requirements related to outcome data that the provider has control over; and (2) consequences related to non-compliance with outcome measurement provisions that the division views as adequate and will enforce.

[The purchaser's contract administration staff may want to pursue whether or not there are other flows of data to the purchaser that is already being received and that could be used to assess outcomes, which could minimize reporting costs by the provider.]

- d. The purchaser's contract administration staff need to use the outcome data, to analyze it and ask questions about it. Nothing undermines the quality of reporting faster than the perception (real or otherwise) by the provider that no one cares about or uses the data being reported.
- e. Consider the range of options available to your agency about how to go about verifying the data being reported. Some potential strategies include:
 - ⇒ "Eyeballing" data for reasonableness.
 - ⇒ Comparing data to data from other entities—again for reasonableness.
 - ⇒ Comparing data to independently known data sources—where possible.
 - ⇒ Going on site to review data collection and summarization processes—the most time consuming method that will need to be employed with judgment regarding the risk of not doing it.
 - ⇒ Requiring that the provider's auditor confirm the accuracy of the data during the provider's annual audit.
- f. Stick to the plan set out under letter (b) above. If the provider has certain action steps throughout the year related to outcomes development and data reporting, follow up and make certain these steps are being taken.

The bottom-line on outcomes is the following:

Making progress in this area has been talked about for years, and some progress has been made. But, further progress won't happen – and the potential benefits from contracting according to outcomes won't accrue – unless top administrators, mid level managers, and contract administrators in purchasing agencies make a commitment to hawk this issue until high quality outcome information is obtained and used.

4 Procurement and sub-contracting requirements

The *Allowable Cost Policy Manual* (Chapter B3 of the *Financial Management Manual*) is the department's policy on the allowability of costs for department programs. This section includes an excerpt from the ACPM which addresses purchase of services.

The ACPM is online at www.dhfs.state.wi.us/grants.

Each agency shall have policy and procedures in place to provide reasonable assurance that the agency's procurement and sub-contracting activities are in the best interest of the agency, considering its responsibilities to the organization, its members, employees, clients, the public at large, and the granting agency. Detailed guidance on procurement and sub-contracting can be found in OMB Circular A-102/Common Rule and OMB Circular A-110. These documents should be consulted when developing or assessing an agency's policy on procurement and sub-contracting.

All care and services purchased by the department, a county social services department, a county department of public welfare, or a board established under sections 46.23, 46.036, 51.42, or 51.437 of the Wisconsin Statutes shall be authorized by a written contract with the provider. For purchases of \$10,000 or less, the requirements for a written contract may be waived upon written request to the appropriate Department contract administrator.

When procuring or sub-contracting under a grant from the Department, an agency will use its own policies and procedures, provided they adhere to the following minimum standards:

- **Written Standard of Conduct** - The agency shall maintain a written standard of conduct that includes a prohibition against any employee, officer, or agent of the recipient participating in the selection, award, or administration of a contract in which financial assistance funds are used, where, to his knowledge, he or his immediate family, partners, or organization in which he or his immediate family or partner has a financial interest or with whom he is negotiating or has any arrangement concerning prospective employment.

Public officials and employees should also be aware of Sec. 946.13 of the Wisconsin Statutes, which prohibits a public official or employee, acting in his private capacity, from negotiating, bidding, or entering into a contract in which he has private pecuniary interest at the same time he is authorized in his official capacity to exercise discretion in making or administering the contract.

Agencies should consult their corporation counsels, or equivalent, if they have concerns regarding conflict of interest.

- **Open and Free Competition** - Procurement and sub-contracting shall be conducted in a manner to provide, to the maximum extent possible, open and free competition.
 1. The agency shall be alert to organizational conflicts of interest or non-competitive practices among contractors that may restrict or eliminate competition or otherwise restrain trade.
 2. Those who develop or draft specifications, requirements, bid invitations, requests for proposals, etc. shall be excluded from competing.
 3. Awards shall be made to the bidder/offeree whose bid/offer is responsive to the solicitation and is most advantageous to the agency.
 4. Solicitations shall clearly set forth all requirements that the bidder/offeree must fulfill in order for his bid/offer to be evaluated by the agency.
 5. Any and all bids/offers may be rejected when it is in the agency's interest to do so.

- **Minimum Procedural Requirements** - Recipients shall establish written procedures that provide for, at minimum, the following requirements:
 1. Procurement and sub-contracting actions shall follow a procedure to avoid purchasing unnecessary or duplicative items.
 2. Solicitations for goods and services shall clearly and accurately describe the goods and services to be procured or sub-contracted.
 3. Some form of price or cost analysis shall be made in connection with every procurement and sub-contract action to ensure that costs incurred are reasonable, that costs are allowable if they are charged to financial assistance programs, and that the agency is not paying for services which are otherwise available free of charge to the agency.
 4. A system of contract administration shall be in place to ensure contractor conformance with terms, conditions, and specifications of contracts or purchase orders.

5 Purchase of services audit guidelines

The *State Single Audit Guidelines* are the state's instructions to auditors of local governments which have federal A-133 audits. This section includes an excerpt from the *Guidelines* which addresses purchase of services.

The *Guidelines* are currently sold in paper format through the Department of Administration's Document Sales and Distribution Section, www.doa.state.wi.us/dsas/docserv/docsales/index.asp. In the fall of 2001, the final version of the 2001 revision to the *Guidelines* will be online at www.ssag.state.wi.us.

Excerpts from two of the documents referenced in this section are included elsewhere in this document:

- The procurement and subcontracting requirements from the *Allowable Cost Policy Manual* (part of the *Financial Management Manual*) are in Section 4 of this document.
- The guidance for identifying and assessing risk from the *Provider Agency Audit Guide* is in Section 8 of this document.

Purchase of service

Background

Section 46.036 of the Wisconsin Statutes establishes the standards for purchases of care and services made by a county social services department, a county department of public welfare, or a board established under s. 46.23, 51.42 or 51.437. Per section 20.002(13) these standards are also applicable to Indian Tribes. Additional purchase of service (subcontracting) requirements are contained in the *Financial Management Manual*, the federal Common Rule, and OMB Circular A-133.

Compliance Requirement

Counties must follow acceptable procurement standards when purchasing care and services using funds from the Department of Health and Family Services.

Suggested Audit Procedures

Determine whether the county:

- procured the care and services through a process that is consistent with applicable procurement policies and procedures.
- has a conflict of interest policy regarding the selection, award, or administration of the contract.
- has contracts on file for purchase of services, where applicable, or a waiver from the

Department of Health and Family Services.

- monitors contract compliance, including collecting financial, performance, program, and special reports; reviewing them in a timely manner; and taking action when problems were noted.
- ensures that payments for care and services do not exceed the amount specified in the contract.

Compliance Requirement

Providers which receive more than \$25,000 in funds from the Department of Health and Family Services must have an audit that meets department standards, unless the audit is waived by the department. The department's standards are in *State Single Audit Guidelines* for local governments with A-133 audits and the *Provider Agency Audit Guide* for all other agencies. Provider audit reports are typically due to the granting agency six months from the end of the provider's fiscal period, and the granting agency should review and resolve the provider audit reports within six months of receipt of the reports.

Because of the timing of audit fieldwork, auditors are likely to encounter situations where the deadlines for when audit reports are due to the county and for when the county must review and resolve the audit reports have not yet passed as of the end of fieldwork. In these cases, there is no finding of noncompliance, and county auditors must follow-up on the status of the provider audits in the subsequent county audit. Guidance on presenting audit findings involving provider audit reports is included at the end of this section.

Suggested Audit Procedures

Determine whether the county:

- documented its decision process, if it used the *Provider Agency Audit Guide's* risk-based approach when deciding whether to require an audit and, if so, the kind of audit.
- performed alternate monitoring, if it planned to rely on alternate monitoring in order to waive the audit or require a lesser-scoped audit than the risk would have otherwise indicated.
- gave the provider information on the nature of funding (federal, state, local, mixture) so the provider could have the appropriate type of audit.
- received the provider audit reports or has a waiver on file from the Department of Health and Family Services.
- reviewed the provider audit reports to ensure they contain all applicable report elements required by the contract and by the type of audit that was performed.
- resolved audit findings within six months of receipt of the audit.

Reporting Purchase of Service Findings in the Schedule of Findings and Questioned Costs

For provider audit reports which have not been received as of the end of fieldwork:

- if the deadline for receiving the provider audit report has not passed, there is no finding of noncompliance. (The auditor follows up in the subsequent county audit.)
- if the deadline for receiving the provider audit report has passed, report a finding in the Schedule of Findings and Questioned Costs.

For provider audit reports which have been received, but not yet reviewed and resolved as of the end of fieldwork:

- if the deadline for reviewing and resolving the provider audit report has not passed, there is no finding of noncompliance. (The auditor follows up in the subsequent county audit.)
- if the deadline for reviewing and resolving the provider audit report has passed, report a finding in the Schedule of Findings and Questioned Costs.

At a minimum, the finding must include:

- the name of the provider,
- the payments made applicable to the contract period,
- the Community Aids Reporting System (CARS) line number on which the related expenditures were reported DHFS, and
- the program title and identification number.

6 Contract review checklist

Over the years, the Office of Program Review and Audit, in the Department of Health and Family Services, has been asked on many occasions to review draft contracts and to offer suggestions on how contracts could be improved. The primary focus of the review typically has been on how to tighten up contract deliverables to better ensure that the expected contract results are clear, unambiguous, and enforceable. However, our reviews have also looked at other contract components.

To help organize and focus our contract review activities, we developed the checklist below. Perhaps by following this or a similar checklist edited to meet a purchaser's unique needs, a purchaser could promote some contracting efficiencies and better ensure that contracts are complete and meet the purchaser's needs.

Contract Review Checklist

- ☐ Clearly defined contract period (start and end date).
- ☐ Complete name and address of Purchaser and Provider, Grantor/Grantee, etc.
- ☐ Clear description of what (goods, services, etc.) is being purchased or contracted for under this contract (may be in contract body and/or exhibits). In order to be effective and enforceable, contract deliverables need to have certain important characteristics. Contract deliverables need to be:
 - ☐ Specific and measurable;
 - ☐ Unambiguously defined so that essential features of desired deliverables are clearly understood, such as how timely something needs to be done or how many of certain things need to happen; and
 - ☐ Linked to broader objectives the purchaser is striving to achieve, such as compliance with federal or state legal requirements, accomplishment of the purchaser's strategic plan objectives, and/or goals established as part of a needs assessment.
- ☐ Name, location, telephone number of contact person for this contract.
- ☐ Contract fully describes the purpose, content, and due dates of program reports that the Provider must submit, which typically will present information showing the extent to which the Provider has achieved contract goals.
- ☐ Clear, concise language or measures that determine how and when the Provider has

achieved adequate performance.

- ❑ Each exhibit attached to the contract is labeled correctly and referenced in the contract body.
- ❑ The maximum amount of funds that the Provider may receive from Purchaser.
- ❑ Clear, concise language describing the payment system and the basis of payment.
- ❑ Provider can expect payments according to the following schedule:
- ❑ If needed, the conditions and terms to withhold or reduce payments due to performance problems/issues are clearly described.
- ❑ If adherence to standards is required in the contract, standards are available for the Provider
- ❑ Reports to the Purchaser are described and related to deliverables, including content and timelines/due dates.
- ❑ Contract states if Provider may or may not subcontract under this agreement.
- ❑ Requirements of Provider and/or Purchaser regarding notice to terminate this contract are clearly described.
- ❑ Any and all items added to the standard contract language are clear, reasonable, and enforceable, and do not contradict other items in the contract.
- ❑ If needed, Special Provisions are stated and clearly defined.
- ❑ Overall: Clear description of expectations, consequences, responsibilities, and obligations for both the Purchaser and Provider under this contract.
- ❑ Notable exceptions to any above item(s):

7 Payment mechanisms

The following material is an excerpt from the department's Contact Administrator's Manual, which is an internal document. This section includes information which may be useful to any contract administrator, although you will find some references are unique to DHFS's environment.

A. Cost Reimbursement

What is a cost-reimbursement payment mechanism?

Traditionally, most DHFS grants have been paid on a cost-reimbursement basis. Contractors submit monthly expense reports for allowable costs incurred up to a maximum level of reimbursement, which is specified in the contract. Allowable costs are those that are reasonable and necessary to achieve the objective(s) of the contract, and are consistent with the provisions of the DHFS Allowable Cost Policy Manual. Most agencies will also have to submit an annual audit to confirm that it complied with state and federal cost policies.

What are the advantages and disadvantages of paying contractors by reimbursing costs?

One advantage to using cost-reimbursement contracts is that established measures exist (for example, the allowable cost policies and annual audits) to confirm the appropriateness of payments. As well, the contractor's costs of reporting expenditure and program information are generally considered low, and the Department is quite efficient at making payments on a cost-reimbursement basis.

However, although payment can be withheld and contracts terminated or not renewed if performance is sufficiently poor, cost reimbursement payment mechanisms provide little or no incentive to perform effectively and achieve the goals of the contract. Contractors don't get paid for what they accomplish, but for what they spend. They also get paid only for allowable costs, which sometimes can be different than needed services, since policy prescribing what's allowable may not keep pace with innovative ways of providing services. Contractors may not be able to offer services clients need, if they are not allowable costs and reimbursable. The contractor also has little or no incentive to be efficient, because any unspent funds must be returned to the Department, even if contract goals have been exceeded.

When should a cost-reimbursement payment mechanism be used?

Cost-reimbursement is used when the purchaser is especially concerned about controlling expenses, and reported costs can be compared to a line item budget that is part of the contract. It is also useful when it is difficult to estimate the cost of providing services and to negotiate a

rate that allows adequate payment to the contractor, while guarding against excess profits.

B. Unit Cost or Fee-for-Service

How does a unit cost or fee for service payment mechanism work?

Under a unit cost or fee-for-service system, the contractor is paid only for the number of units of service provided at an agreed-upon price per unit, or rate. Units of service are typically program outputs, such as number of hours of counseling or training sessions provided.

When should a fee-for-service payment mechanism be used?

Fee for service payment systems generally work best when the amount of service needed is predictable and the cost of providing the service is known. The contract should ensure the contractor is not allowed to bill for more services than there are funds available to pay for. Sometimes the maximum amount of reimbursement a contractor can receive will be specified in the contract, and the contract agency will either need to stop providing services when the maximum is reached, or else cover these additional costs from other sources.

What are the advantages and disadvantages of fee-for-service arrangements?

If there is competition between potential contractors, fee-for-service arrangements should encourage efficiency and lead to reasonable fee levels, and may even make it possible to purchase services at a discount. However, if there is only one appropriate contractor, and competition cannot be relied on to drive prices down, it is still necessary to make sure the Department is "buying smart" and paying the lowest reasonable price for the service. This might require doing an analysis of the actual cost of providing the service, and/or by doing a market comparison with similar services.

Fee-for-service payment rewards contractors that maximize the number of units of service provided, as long as they control other costs. This incentive to provide increasing amounts of service may encourage the provision of unnecessary services and could result in the Department being committed to spend funds in excess of the available budget. To avoid this, it may be necessary to place controls on the demand for services or on the amount of services that can be billed. It might also be useful to incorporate other incentives, such as the achievement of certain results, rather than only rewarding the provision of more services. Without adequate controls, the threat of service demands exceeding budget is very real, and should be considered carefully before using fee for service as a payment option.

Fee-for-service can also have an adverse effect on the quality of services, since it provides incentives for contractors to keep costs low in order to generate more revenue. The contract administrator thus needs to have an on-going system of assessing the quality of services being provided.

C. Capitation

How do we pay contractors under a capitated payment system?

Under a capitated model, the contractor is paid a certain amount to provide defined services to a target group, and is held accountable for providing the required services despite the final cost. This type of payment mechanism has been most widely used in the medical service field, and to a lesser extent in mental health and substance abuse services.

Capitated payments are often associated with managed care models of service delivery. For example, a monthly payment is made on behalf of each of a medical managed care organization's enrollees regardless of whether they receive frequent or expensive services during any given month, or no services at all. The managed care organization is responsible for managing the care of these patients, and may risk losing money if total expenses exceed the pre-determined amount of funds.

How are capitated rates determined?

Capitated rates are estimates of the costs of service consumption, based on historical information and assumptions about the future. The development of reliable capitation rates requires the involvement of many disciplines both within and outside the Department, to develop a complete specification of the services to be provided, predict the number of clients who will be using various levels of the services, and estimate the cost of providing the expected volume of service.

Typically, services of an actuary are heavily relied on to estimate what it would cost to serve the target population under a fee-for-service arrangement. That cost is then used as a benchmark in determining the amount of the capitated payment. This process requires a longitudinal database of utilization and expenditure information, which must be verified for completeness and accuracy.

Although capitation does not necessarily result in savings, it is generally presumed that capitated rates will be set so that less total funds will be expended for the same services than if other payment mechanisms are used. For example, the Department may set capitated rates for Health Maintenance Organizations serving AFDC clients at 92% of the projected fee-for-service costs.

How do we know if the capitated rates are accurate?

Ideally, capitated rates accurately predict the actual costs of providing services to the target population. In reality, since they are basically projections of future events, it is realistic to expect they will not be 100% accurate, and that actual costs may be either higher or lower than predicted. Because of this, Department capitation contracts may provide for a retrospective review process, conducted after the services have been provided, to determine what the actual costs of providing them were. This review may

also focus on the appropriateness, necessity, quality and reasonableness of services provided.

How is the financial risk managed if capitated rates are not accurate?

Until the accuracy of the capitated rates has been demonstrated, a contractor will probably not be willing to assume the financial risk if it turns out they do not adequately cover the costs of service delivery, and the Department will probably not be willing to assume the risk if the rates are high and generate excess profits for the contractor. For this reason, the purchaser (DHFS) and the provider usually agree to some sort of risk sharing mechanism for a period of time, perhaps several years, while the program evolves and the rates are refined. In some situations, DHFS may assume all the financial risk. Once the Department and contractor have confidence in the accuracy of the rates, the contractor may be expected to manage costs within the capitated rate.

What are some ways that the financial risks entailed in capitated payment mechanisms can be shared?

In order to protect both contractors and the Department, a variety of risk sharing mechanisms can be used, including:

- Tiered risk sharing -- the state and the contractor each assume a portion of the loss, depending on what percentage of total revenues the loss is. This method can also be applied to the sharing of excess revenues;
- High risk pools -- the state agrees to cover the cost of particularly high-cost "outlier" clients. Monitoring mechanisms must be established to verify claims on the risk pool. The risk pool may be reduced as the Department fine tunes the rate-setting process and as the provider organization gains experience in implementing a capitated system of service delivery;
- Reinsurance -- the provider organization purchases an insurance product that protects it from high outlier costs. Reinsurance can be limited to costs associated with a specific service such as inpatient hospital costs, or it may cover total aggregate costs that exceed a certain amount; and
- Risk reserves -- the contractor maintains sufficient financial reserves to assure program financial viability in the face of operating deficits. For example, health maintenance organizations operating in Wisconsin must have a net worth of \$750,000, or 3% of the prior 12-month's premiums, in a reserve account. Other managed care programs contracting with the Department have been required to maintain risk reserves equal to two months of capitated payments.

Is capitation used as the only payment mechanism in a contract? Or can it be combined with other payment options?

Even where a capitation rate is used, a contract may identify certain services that will be reimbursed on a different basis. For example, there might be some services that contractors are unwilling to provide without a guarantee that their actual costs will be covered, either because they are very expensive, or because it is difficult to establish a sound actuarial basis for them. For example, medical services for individuals infected with HIV have sometimes been carved out of capitated contracts for medical services, and paid on a fee-for-service basis. In addition, there may be financial penalties for failure to meet certain service level targets even though reimbursement is made on a capitation basis.

What are the advantages and disadvantages of capitated payment systems?

If there is competition among contractors, it pushes them to manage more efficiently and provide services less expensively than under fee-for-service arrangements. The marketplace also helps control cost and quality of services, since consumers can "shop around" for providers that best meet their needs.

There are also some disadvantages to this model, however. If enrollment is voluntary, contract agencies may be tempted to "cream", or try to serve the least costly clients, while avoiding those who are most costly. It is possible to include contract language that makes it more difficult for contractors to focus on "easy" clients. On the other hand, providers who offer high-quality services may attract the needier and higher-cost clients, and it may be necessary to adjust their rates. Also, once a rate has been determined, it is in the interests of the contractors to hold down costs as much as possible, and they may attempt to increase profits by reducing the quality or quantity of services, to the detriment of the recipients of those services. Without performance standards in the contract, there is no guarantee that some recipients may not receive what they need.

In the health care field, where capitation is used extensively, there are standards for service provision, licensing systems for professional providers, and credentialing protocols for staff of health maintenance organizations that furnish at least some level of quality assurance over the services provided. But whether in health care or in other program areas, where quality assurance procedures may not be as well established, it is always necessary to monitor the services provided to ensure they are of acceptable quality. Developing performance expectations, and then establishing the monitoring systems needed to assess performance, suggest an added cost factor that needs to be considered when using this form of payment mechanism.

D. Performance-Based

What is performance-based contracting?

Performance-based contracts focus on and pay for results, as indicated by performance measures. "Performance" can be measured in terms of program outputs, outcomes, or a combination of the two. Outputs typically focus on the processes of service delivery, while outcomes focus on the results the provided services are intended to achieve. To the extent that performance measures are based on outputs alone, such as clients receiving services, this kind of payment system is not materially different from a fee-for-service system.

The outputs or outcomes that are used as performance measures are developed using the same method described for developing program objectives, in the last section. In all likelihood, the performance measures that payments will be based on will be chosen from the program outcomes and objectives already developed.

How do we decide if we should use a performance-based contract for a particular program?

Since performance-based contracting addresses critical issues of program accountability and effectiveness, a strategic business goal of the Department is to base increasing portions of payments on achieving performance goals. Performance-based payment mechanisms should be considered when:

- It is desirable to provide an incentive for good performance or a disincentive for a failure to produce those results. For example, one way to accomplish this could be by reimbursing 90% of reported costs, but holding back the final 10% unless or until certain results were achieved. The major advantage of this kind of payment mechanism is that it provides an incentive for the contractor to accomplish the program objectives specified in the contract, since a failure to produce results reduces the payment received;
- It is possible to establish measurable performance criteria, whether outputs or outcomes, that indicate whether the program goals are being met. Some programs may be too multi-faceted for a few indicators to reliably indicate adequate performance; or
- The time invested in determining the level of payment based on performance indicators will be worth the payoff. If the entire program is small, or if only a small portion of a contractor's payment is going to be tied to performance, it may not be worth the time involved. Deciding not to base payment on specific objectives does not mean the contractor will not be held accountable for meeting those objectives. Information on program outcomes and progress being made to meet all contract goals and objectives will still be reported on by the contractor and monitored by the contract administrator, it will just not be used as a basis for making payments.

Are performance-based payment mechanisms ever used as the only way to pay contract agencies, or are they combined with other payment methods?

For a variety of reasons, the Department has not used a payment mechanism which is based totally on achieving outcome measures; however, it is possible to integrate performance-based

payment into other payment methods. For example, performance and cost-reimbursement payment mechanisms have been combined in making payments to many providers in the Child Welfare program in Milwaukee County. The Department also has introduced performance objectives with fiscal consequences in capitated payment contracts with HMO's in the Medicaid program.

Is it possible for a non-profit organization, which may have limited funding and isn't supposed to make any profit, to enter into a performance-based contract?

Although they don't make profits, which would go to owners or stockholders, non-profits may have reserve funds from donations or other sources. These reserve funds could theoretically be used to pay program costs not covered in other ways, or to receive bonuses or additional money earned for exemplary performance. It is true that small, community-based organizations may not have the same ability to assume risk under a performance-based contract as do larger, more diversified organizations, however, and specific payment provisions will need to be carefully thought-out for each situation.

How does DHFS process payments that are based on performance? Who determines whether the contractor has met performance goals, and how much they should be paid?

Performance-based contracting is a relatively new process for DHFS. It will probably be necessary to consult with the CARS unit to be sure the payment mechanism included in the contract is one they can implement.

As the person with the most knowledge of the program area, the performance measures in the contract, and the contractor's actual performance, it is presumed the contract administrator will need to determine the appropriate payment and to communicate this with the CARS unit, which will then make the payment

Are there any problems or issues to consider about performance-based contracting? How can these issues be addressed?

Below is a discussion of problems that may emerge when purchasers reward contractors based on a performance contract. Possible solutions to the problems are included in the discussion. The complexities involved in performance-based contracts will necessitate discussions with bureau and division program staff and managers, who may also want to involve staff from OPRA, OLC and/or BFS.

- Performance measures cannot account for all of the factors that affect program outcomes, some of which are beyond the control of service contractors and program staff (e.g., demographics and economic conditions). Contractors and program staff must be given an opportunity to report the context, including items such as client characteristics, in which their programs operate, or they will be tempted to "cream," and provide services only to the easiest clients or cases. For instance, one way for adoption agencies to make their performance look better is to work with those children most

likely to be adopted. Ways to avoid this situation are:

- Include a definition of the target group in the contract. For instance, rather than paying for all completed adoptions, the contracting agency might pay only for adoptions of special needs children, or children who have been in foster care for a certain length of time; or
- Reward contractors for accepting difficult clients. For instance, clients could be identified as having a higher or lower functional rating, and outcomes or payments could be different for those with higher needs.
- Providers might try to negotiate easy outcomes. For instance, if a child who has been in foster care goes back to his/her own family, this does not mean the child will not need to be placed in foster care again. More sophisticated performance contracting would provide financial incentives to agencies that return children to homes that provide adequate care and stability for a certain period of time.
- The minimum expectation may become the maximum. In other words, there is no incentive to perform above the minimum level required to fulfill the contract requirements. In this case, the purchaser should use different rates for different levels of outcomes, or write a contract that specifies the specific level of outcome expected. For instance, if an improvement in reading grade level during treatment is the objective, the contract should specify the expected grade level improvement. Contracting for an "improvement" in grade level will not provide sufficient motivation for the contractor to help the child improve above a minimal amount that meets the contract requirement.
- Contractors might argue over the rules. If contractor's know there may be a penalty for failure to achieve contracted outcomes, they may argue about how the decision was made to withhold an incentive and what evidence was used to determine that the outcome was not achieved. For this reason it is necessary to use outcomes that are observable and measurable: Two people should be able to look at available documentation and agree that the outcome was or was not achieved.
- Providers may focus only on those objectives with monetary or other rewards, and not on the overall goals of the program. To avoid this situation, make sure the measure used to determine payment is an important indicator of overall performance, or use a set of outcomes, rather than a single outcome, to determine payment.
- There may be resistance to new reporting requirements. If so, it may be possible to make these requirements more palatable by pointing out that the data necessary for performance contracting is also information that should be routinely collected as part of good program management, and having this information available will allow program staff to improve the program and make it more competitive for future contracts.
- The additional work in performance contracting will be in negotiating the agreement and in assuring that documentation is accurate and reliable. This may mean more contract administrator involvement in monitoring performance,

however the pay-off in terms of improved program performance and increased accountability may be worth the extra effort.

- Providers may be reluctant to enter into performance-based contracts, since they have potential for disrupting the agency's funding stream. Small agencies may have little or no financial reserve to depend on if they do not earn as much as they expected to. Also, the contractor needs to have some way of generating revenue while trying to produce the desired results. This effect can be cushioned by using interim performance measures, or by making only a portion of payment contingent upon performance and continuing to pay partially on the cost-reimbursement model.

The more complex the business requirements in the RFP/RFB and contract, the less likely it is that potential contractors will be interested. Department staff may need to take the initiative to seek out providers that are willing to enter into performance contracts, and consider phasing in performance contracting over a period of time.

8 Identifying and assessing risks

The *Provider Agency Audit Guide* is the department's policy for audits of non-profits, for profits, and certain local governments (those which do not need A-133 audits). The references in this excerpt are to other sections of the *Guide*, which is online at www.dhfs.state.wi.us/grants.

All providers which receive department funding in excess of the statutory threshold for requiring an audit (Appendix B) need to have an agency-wide audit *unless* the granting agency chooses to use this chapter's risk-based approach either to waive the audit or to require a lesser scoped audit. Examples of situations where the granting agency may choose not to use the risk-based approach include when it knows the provider needs to have a single audit in accordance with OMB Circular A-133 or when it requires agency-wide audits as a matter of policy.

Under the risk-based approach, the granting agency matches the monitoring and auditing methods to the risk that a provider will have problems in administering a contract for the purchase of care and services. The risk factors are in three categories:

- 2.1 Risks associated with a particular program
- 2.2 Risks associated with a particular provider
- 2.3 Risks associated with the granting agency

The granting agency determines whether the risk factors point toward lower or higher risk and uses the results of these individual factors to assess whether the provider's overall risk is low, moderate, or high. After the granting agency identifies and assesses risks, the next step is to select the type of audit that best complements the granting agency's other monitoring efforts. That step is covered in Chapter 3.

When the granting agency chooses to use the risk-based approach, it must perform the risk assessment in a systematic and rational manner, and it must document the risk assessment. Illustration 2.1 "Risk Identification and Assessment Worksheet" offers one approach to performing and documenting a risk assessment. Granting agencies may choose to develop their own risk assessment tools based on the content of this chapter. They may also choose to add other risk factors or to assign some risk factors more weight than others. The granting agency's auditor will test the granting agency's assessment of risks for its providers as part of the audit of the granting agency, and the audit procedures for testing risk assessment are in Section 5.1.1.

The granting agency should perform the risk assessment at the time it is considering whether to contract with the provider. This offers several benefits:

- The granting agency is likely to consider some of the same risk factors, such as the provider's experience and past performance, when deciding whether to contract with the provider.

- The granting agency can specify special reporting or monitoring requirements in the contract.
- The granting agency can specify the type of audit in the contract.

The provider's auditor may find the risk factors described in this section useful during audit planning, especially when selecting programs for program level testing in an agency-wide audit (Section 4.3). In addition, the granting agency should make its risk assessment available to the auditor, so that the auditor can take the granting agency's concerns into account while planning the audit.

Illustration 2.1 Risk Identification and Assessment Worksheet

Risk Factors		(Place a checkmark next to the description that best suits the risk factor)	
		Lower Risk	Higher Risk
2.1	Program Characteristics:		
2.1.1	Lifestage of the program	More than two years	Less than two years
2.1.2	Complexity of the program	Low level of complexity	High level of complexity
2.1.3	"Sensitivity" of the program	Low level of sensitivity	High level of sensitivity
2.1.4	Who decides eligibility for the program	Granting agency	Provider
2.1.5	Who decides amount or type of service from the program	Granting agency	Provider
2.1.6	Payment method	Unit-times-unit-price and granting agency has independent means of knowing reasonability of price and number of units.	All other payment methods
2.1.7	Competition	Competitive basis	Not competitive
	Other characteristics:		
2.2	Provider Characteristics:		
2.2.1	Provider's total funding from the department	Less than \$75,000	Greater than \$75,000
2.2.2	Provider's length of time in business	More than two years	Less than two years
2.2.3	Provider's experience and past performance	Extensive experience and history of good performance	Little to no experience or history of problems with performance
2.2.4	Provider's financial health and practices	No financial difficulties or problems with financial practices	Financial difficulties or problems with financial practices
2.2.5	Provider's compliance and internal controls	No problems	Some problems
2.2.6	Provider's fiduciary responsibilities	No fiduciary responsibility	Provider has fiduciary responsibilities
2.2.7	Provider's subcontracting	Little to no subcontracting or effective contract monitoring function	Extensive subcontracting or ineffective contract monitoring function
	Other characteristics:		
2.3	Granting Agency Characteristics:		
2.3.1	Granting agency's experience with the provider agency	Extensive experience	Little to no experience
2.3.2	Granting agency's experience with the program	Extensive experience	Little to no experience
2.3.3	Granting agency's monitoring methods	All significant risks covered by alternate monitoring	Some significant risks not covered by alternate monitoring
	Other characteristics:		
Overall risk assessment:		Low risk	
		Moderate risk	

	High risk
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2.1 Risks associated with a particular program

Programs differ in their inherent risks, which include:

- 2.1.1 Lifestage of the program
- 2.1.2 Complexity of the program
- 2.1.3 “Sensitivity” of the program
- 2.1.4 Who decides eligibility for the program
- 2.1.5 Who decides amount or type of service from the program
- 2.1.6 Payment method
- 2.1.7 Competition

In addition to the factors listed in this section, the department may have identified risks specific to certain programs. In some cases, the department will send granting agencies alerts or other program bulletins describing the issues it is concerned about. The department’s contract administration or audit staff (Appendix A) are also good sources for information on risks for particular programs.

2.1.1 Lifestage of the program

Established programs generally have less risk than newer programs would have. In addition, recent significant changes to an established program can increase risk.

2.1.2 Complexity of the program

Programs that have simpler requirements (eligibility, calculations, reporting) generally have less risk than programs that have more complex requirements.

2.1.3 “Sensitivity” of the program

The “sensitivity” of the program is made up of two factors: the vulnerability of clients and the visibility of the program. Programs that serve vulnerable clients generally have higher risk because these clients might not be able to convey to others that they are not receiving adequate services. High visibility can cut both ways: while any problems are more likely to become apparent, which reduces risk, any problems that do occur can quickly harm the credibility of both the provider and the granting agency, which increases risk.

2.1.4 Who decides eligibility for the program

Risk is lower when the granting agency determines eligibility, and it is higher when the provider agency determines eligibility.

2.1.5 Who decides amount or type of service from the program

Risk is lower when the granting agency determines what services a client gets, and it is higher when the provider makes these decisions.

2.1.6 Payment method

All payment methods have risks, although some are inherently more risky than others depending on the circumstances. Most payment methods are a variant of one of four basic methods of making payments to providers:

- **Cost-based contract** – In a cost-based contract, the provider reports costs to the granting agency, who reimburses the costs. Cost-based contracts include those where
 - The provider is reimbursed for its costs.
 - The provider is responsible for the cost of providing care and services up to a certain amount, after which the granting agency shares in the cost or assumes full risk of the cost overruns.
 - The provider's reimbursement is limited by allowable costs, such as the agency maintaining a reserve (Section 7.1.6).
 - Actual allowable cost information is needed for federal reporting purposes, such as group homes and child caring institutions (Section 7.1.5).

A cost-based contract can have high risk if the granting agency does not have means of ensuring that the provider is claiming only allowable costs for reimbursement.

Some of the risks of inappropriate payments for a cost-based contract include unallowable costs resulting from:

- Inaccurate cost reports.
 - Misallocation of costs or cost shifting.
 - Lack of approval for costs.
 - Inappropriate or unnecessary items.
 - Lack of documentation for costs.
- **Units-times-unit-price contract** – Under a unit-times-unit-price system, the provider and the granting agency decide on a per unit price for the service, the provider reports the number of units of service to the granting agency, and the granting agency pays the provider for the number of units items the price per unit. A unit-times-unit-price method can have high risk if the granting agency does not have means of ensuring that the unit price is reasonable and that the number of units the provider claims to have supplied is accurate.

Some of the risks of inappropriate payments for a unit-times-unit price contract include:

- Inaccurate count of units.
 - Price is too high or too low.
 - Unnecessary units.
 - Undocumented units.
- **Performance-based contract** – Under a performance-based contract, payments are tied to achieving performance goals. Developing performance measures that promote the intent of the program without introducing additional risks to the program can be very difficult, and successful use of this contracting method requires careful planning. Some of the risks of

inappropriate payments for a performance based contract include shift of focus from overall program purpose to measured activities and inaccurate performance reports.

- *Capitated contract*¹ – In a capitated contract the driver for payment is reported eligible enrollees. The contractor is paid a certain amount to provide services to a target group, and it is held accountable for providing the services despite the final cost. There are two types of capitated contracts:

Full risk – the provider is responsible for all costs of providing the care or services.

Shared risk – the provider is responsible for costs of providing care and services up to a certain amount, after which the granting agency shares in the costs.

Some of the risks of inappropriate payments in capitated contracts include:

- Rates set too low or too high,
- Inaccurate reporting of number of eligible enrollees or services provided to enrollees,
- Reduction in costs through reduction in level of services or types of services provided to enrollees, and
- For shared risk capitated contracts, also see the risk factors associated with cost-based contracts (See cost-based contracts, above).

Granting agencies can affect the relative amount of risk by selecting a payment method that suits the particular circumstances. For example, if the granting agency has a program that it does not have much experience with, a unit-times-unit-price contract can be very risky unless there is a means of ensuring that the unit price is reasonable. One way to mitigate this risk is to use a cost-based contract for the first few years to establish a base line for costs.

2.1.7 Competition

Grants that are awarded on a competitive basis are generally lower risk because the competitive process helps reduce the likelihood that the granting agency will be overcharged for the service provided under the grant. Some characteristics of awards made on a competitive basis include:

- The granting agency has a written conflict of interest policy, which it follows in making the award.
- The award is made as a result of a written bid.
- More than two providers bid on the award.
- The granting agency has credible, independent means of knowing that the price is reasonable, not only whether the price is too high, but also whether it is too low to

¹ Wisconsin Statutes allow capitated contracts only for certain services funded by the Medical Assistance program. Contact the department (Appendix A) if you have questions about the allowability of a contract method

support an acceptable level of services.

- As part of the bid process, the granting agency identifies and evaluates the level of services to be provided.

2.2 Risks associated with a particular provider

Providers also have inherent risks. Some of the risks associated with particular providers include:

- 2.2.1 Provider's total funding from the department
- 2.2.2 Provider's length of time in business
- 2.2.3 Provider's experience and past performance
- 2.2.4 Provider's financial health and practices
- 2.2.5 Provider's compliance and internal controls
- 2.2.6 Provider's fiduciary responsibilities
- 2.2.7 Provider's subcontracting

2.2.1 Provider's total funding from the department

A good starting point in considering risk associated with a provider is the total amount of department funding that the provider receives from all sources. The amount of funding is a measure of the amount of the department's exposure if the provider has problems administering programs. Smaller amounts of funding correspond to lower exposure, and thus lower risk, while larger amounts of funding correspond to higher exposure and risk. However, the level of funding is just one many factors that feed into risk. In other words, a provider that was paid \$50,000 is not automatically low risk, and a provider that was paid \$175,000 is not automatically high risk.

Since exposure is considered from the department level, all sources of department funding need to be taken into account. This funding can be direct from the department or passed through one or more of the agencies.

The statutes establish a threshold for when an audit is required unless the audit is waived by the department (see Appendix B for the information on the statutes and Section 3.2 for information on waiving an audit). In addition to the statutory threshold, the department has established the following guidelines for risk for different levels of funding:

Table 2.2 Risk Associated With Total Department Funding

Amount of department funding from all sources	Risk
Less than the statutory threshold (Appendix B)	Audit not required
More than the statutory threshold and less than \$75,000	Lower
More than \$75,000	Higher

2.2.2 Provider's length of time in business

An agency that has been in business for several years will generally be lower risk than a start-up agency. A granting agency can mitigate these risks by performing additional monitoring for new providers.

2.2.3 Provider's experience and past performance

The provider's experience and past performance are key factors in risk: extensive experience and a history of good performance generally means lower risk, while little to no experience or a history of poor performance generally means higher risk.

2.2.4 Provider's financial health and practices

Providers which have good financial health and sound financial practices generally have lower risk. Providers have higher risk if they have trouble paying their bills or if they are in danger of going out of business due to poor financial condition. Providers also have higher risk if they "self deal," attempting to circumvent limits on allowable profits or reserves by doing business with related parties. The granting agency should consider the following questions:

- Does the provider have a history of financial difficulties?
- Does the provider do a significant amount of business with related parties and, if yes, does this business affect department funds?

2.2.5 Provider's compliance and internal controls

A provider with a history of compliance and good internal controls generally is lower risk than a provider with a history of problems in compliance or internal controls. Some questions to answer in assessing the provider's compliance and internal controls include:

- Does the provider's audit report show weaknesses in internal controls that an unscrupulous employee could take advantage of?
- Does the provider's audit report show findings of non-compliance with requirements that relate to department programs?
- Do the same findings recur year after year? This could be a sign that management has not made a commitment to improving operations or ensuring compliance with the terms of the contract.
- Does the provider have adequate segregation of duties? If not, does the provider have effective compensating controls?

2.2.6 Provider's fiduciary responsibilities

Providers which have fiduciary responsibilities for resident funds, such as protective payee, have higher risk than providers which do not have such responsibilities. See Section 5.1 for guidance on auditing fiduciary responsibilities for resident funds.

2.2.7 Provider's subcontracting

Subcontracting affects risk because the subcontractor performs program functions, but the provider remains responsible for compliance with the terms and conditions of the contract with

its granting agency. Risk is higher if the provider subcontracts material activities to other agencies. Risk is also higher if the provider does not have an effective monitoring function for overseeing these contracts. See Section 5.1 for guidance on auditing a provider's subcontracting function.

2.3 Risks associated with the granting agency

The third area of risk is inherent risk of the granting agency itself. Granting agencies differ in their experience in contracting with particular programs or providers and in the availability and effectiveness of their monitoring efforts:

- 2.3.1 Granting agency's experience with the provider agency
- 2.3.2 Granting agency's experience with the program
- 2.3.3 Granting agency's monitoring methods

2.3.1 Granting agency's experience with the provider agency

Contracting with a provider that the granting agency has done business with before generally means lower risk than contracting with a provider the granting agency hasn't done business with before.

2.3.2 Granting agency's experience with the program

The granting agency having extensive experience with the program generally means lower risk than does the granting agency having little or no experience with the program.

2.3.3 Granting agency's monitoring methods

Risk is lower overall when the granting agency has monitoring methods that effectively mitigate the other risks identified in this section. The granting agency must balance the consequences of something going wrong with the costs of the measures to prevent or detect that problem. In doing so, the granting agency may choose to increase its other monitoring efforts so it can waive the audit or require a less extensive audit than the risks would otherwise indicate. However, due to the inherent limitations of audits, a granting agency cannot rely just on audits and forgo other monitoring efforts.

Some of the possible monitoring efforts include:

- Providing technical assistance to the provider on understanding and meeting the granting agency's expectations.
- Reviewing financial reports and claims for reimbursement for reasonability and mathematical accuracy before authorizing payment.
- Requiring supporting documentation for claims for reimbursement.
- Reviewing performance reports and correlating them to financial reports and claims for reimbursement.
- Making site visits to observe services being delivered and to review program records.

- Surveying clients (or their families or caseworkers) on satisfaction with services and responding to complaints about inadequate services.
- Following up on complaints from whistle-blowers.
- Paying attention to media stories on the agency.
- Performing background checks on key staff at the provider agency. (In addition, state law requires background and criminal history checks of certain personnel who are responsible for the care, safety, and security of children and adults. See the Department of Health and Family Services home page (Appendix A) for more information on the statutory requirements for background and criminal history checks.)
- Obtaining references or performing other checks to confirm that key agency staff have sufficient experience to administer the contract.
- Requiring a provider to engage in on-going quality improvement or quality assurance efforts and receiving and reviewing the results of these self-improvement initiatives.

The granting agency should perform a thorough internal review of its monitoring efforts to confirm that the scope and methods of monitoring combined with the extent of audit coverage provide sufficient oversight given the risks involved. The granting agency can use the audit program that the granting agency's independent auditor would use when performing the audit of the granting agency as a starting point for such a review (Section 5.1.1).

9 Site visit tool for monitoring subgrantee performance

The *Financial Management Manual* is the department's policy for financial management practices for programs administered by counties, tribes, and 51 boards. The FMM is online at www.dhfs.state.wi.us/grants.

Whenever one organization contracts with another organization to provide program services, the organization providing the funding assumes some responsibility for assuring that the funds are being managed efficiently and effectively to accomplish the objectives for which funds were provided.

There are several mechanisms that can be used for monitoring performance. Some of these mechanisms include: (a) reviewing and approving program planning documents, (b) reviewing and approving operating budgets for the programs, (c) reviewing and approving expenditure reports for the program, (d) reviewing any reports of program accomplishments or other indicator data on the programs, (e) requiring, reviewing, and resolving audits of the program, and (f) performing on-site visits.

From time to time, in fulfilling its management monitoring responsibilities for subrecipient organizations funded through this department, DHFS staff have conducted on-site visits for the purpose of obtaining a brief assessment of the management capabilities of organizations it funds.

Numerous on-site review tools and performance checklists have been developed for the purpose of assisting staff responsible for monitoring the performance of subrecipients. Recently, however, Office of Program Review and Audit staff have developed a checklist of questions covering the areas of board oversight, financial management, and program management that we have found helpful in developing a broad assessment of organizational performance. This "site tool" is provided as a source of guidance for those whose responsibilities include the monitoring of the organizations to which they provide funds, and who do not already have a tool developed or are interested in reviewing their existing site monitoring tool.

Site Visit Tool For Monitoring Subgrantee Performance

This tool was developed for brief (ideally one day) site visits to provider organizations to enable one to get a feel for how well the organization is functioning. The three broad areas covered are board activities, financial management, and program management.

Depending on the many varied circumstances surrounding the program(s) and provider organization being monitored, the users of the tool need to decide which of the enclosed questions are applicable, whether other subject areas need to be included in the review, and the criteria the reviewer(s) will use to determine whether the answers offered by the provider organization are acceptable. For example, if a recently completed comprehensive financial audit of an organization identified no accounting problems, the reviewer(s) may not need to ask every question pertaining to financial management. On the other hand, knowledge of past program performance concerns may prompt the reviewer(s) to concentrate on obtaining full and complete answers to all program management questions.

Board Activities

1. Are there Board approved by-laws? Obtain copies and review for relevant materials.
2. Are there Board approved personnel policies and procedures? Review these for any items that may be relevant to program operations or to the costs charged to grant programs.
3. Is there a Board approved financial policy and procedures manual? Is it updated on a periodic basis?
4. Determine the Board's role in establishing program directions, including development of a mission statement for the organization.
5. What kind of financial and program performance reports typically go to the Board, if any?
6. How active a role does the Board take in financial matters? In reviewing budget priorities? In reviewing financial performance?
7. Has the Board established performance goals for the Executive Director and periodically evaluated performance of the Executive Director?

Financial Management

1. Does the agency charge indirect costs to grants? If so, do they have a written indirect cost plan? Is the pool of indirect costs to be recovered through the rate segregated

from costs charged directly? Are indirect costs budgeted for and approved in grant contracts? Do the costs charged meet any limitations prescribed for indirect costs?

2. Does the agency allocate costs? If so, is there a written cost allocation plan? Is it reasonable? Is it followed?
3. Are the agency's bank statements reconciled in a timely manner? Check for signatures and for the age and amount of outstanding checks.
4. Are the agency's expenditure reports, which are submitted to the granting agency, supported by the agency's accounting records? Consider the rate of expenditure of granting funds. (The subgrantee may not be adequately controlling funds if year-to-date expenditures, when annualized, far exceed budgeted amounts. On the other hand, expenditure rates well below budgeted levels may indicate the subgrantee is not meeting targeted service levels.)
5. Is there adequate supporting documentation in the accounting records to support transactions that appear in the accounting system? Records of original entry, journal entries, correction transfers. (For a quick review, ask to see where these are kept and select a few samples of each of these and review with the business office staff how these are prepared and see what types of support are attached to the copies that appear in the files.)
6. What kinds of records make up the agency's accounting system? Detailed, summary, management. (For a quick review, select a few entries that appear on a recent expenditure report that has been filed with the department and ask the business office staff to trace back through the worksheets used to prepare the report and the associated accounting records from which the numbers on the worksheet were taken. This process is not overly time-consuming and can provide one with a quick comfort reading on the agency's record keeping system.)
7. Has the subgrantee developed and followed through in implementing a corrective action plan designed to fix all accounting deficiencies noted in the subgrantee's last annual audit?
8. How are the agency's individual grants accounted for in the accounting system? What records are kept of grant activity?
9. Is the subgrantee experiencing difficulties paying bills in a timely manner, as would be evidenced by a substantial amount of outstanding payables? If so, how old are the unpaid bills?
10. Are any program services offered through subcontractors? If so, review the subcontractor contracts and the status of payments to the subcontractors.
11. Does the organization keep records of equipment purchased with grant funds which show the date and amount of purchase, a description of the equipment which would

enable one to identify and locate the particular items listed, and the grant sources which contributed to the purchase along with the amounts contributed by each?

12. Review any major leases for space and equipment to ensure that the amount ultimately charged to grants for such items are reasonable and to identify any related party transactions that might result in unreasonable charges to grants for these items.

Program Management

1. Are there current, specific position descriptions for staff and supervisors?
2. Are there provisions for employee evaluations, and is there evidence that employees are evaluated regularly?
3. To what extent do Program Directors manage their programs? That is, to what extent are program directors: (a) seeking out additional support for new programs related to their existing programs; (b) developing program plans; (c) monitoring operating budgets; (d) setting program priorities; and (e) preparing any reports of program accomplishments?
4. What financial reports do program managers routinely use?
5. Do program managers have a clear idea of their program objectives?
6. Have program managers developed measures of success which indicate the degree to which program objectives are being met? Is this information presented to the board? Is the information used by the organization to improve program services?
7. Check contracts for performance goals and determine the extent to which these are being measured and met.
8. How often do monitoring staff review the programs operated by the organization? What programs are reviewed? Are there any reports on the results of monitoring visits? What do the reports have to say about the programs?

10 Monitoring performance, renewing or closing out contracts, and audits

The following material is an excerpt from the department's Contact Administrator's Manual, which is an internal document. This section includes information which may be useful to any contract administrator, although you will find some references are unique to DHFS's environment.

I. Start-up and Implementation.

A. Sometimes the contract administrator isn't appointed until after the contract is developed and the provider is selected. In that case, what does he/she need to know to get started?

First of all, the contract administrator needs to make sure he/she has on hand and is familiar with all rules and regulations pertaining to the program which is the subject of the contract. Sources of contract requirements, also listed in Section One, III, could include:

- Federal laws and regulations;
- State statutes, legislative language;
- Administrative rules;
- Department policies;
- Division Administrator memos;
- Catalog of Federal Domestic Assistance (CFDA);
- Notice of grant awards; Applications for grants; and
- Program requirements.

The contract administrator should also read all available documents relating to the contracting process -- the RFP or RFB, the contractor's bid or proposal, any significant correspondence relating to the establishment of the final contract, and the contract itself. The contract administrator also needs to make sure he or she is aware of any issues that may have come up in the contracting process to date. Issues to explore with those who were involved (program, budget, legal, etc.) include:

- The existence of any controversy in the contracting process;

- The nature of the negotiations -- did they go smoothly or were there significant tensions?
- What issues were problematic?
- The possible existence of any verbal promises made outside the scope of the contract; and
- Concerns regarding the contractor's ability to perform.

B. What information should the contract administrator keep on file?

Division or bureau practice may be to keep the RFB/RFP, along with the chosen contractor's response and the complete contract in a central file. In this case, the contract administrator should know where they are kept, so they can be referred to. Other items should be kept by the contract administrator. All contract files can be considered public documents, and proper discretion should be used when documenting communications with or about contractors.

The following are items that should be kept in the contract file or files:

- Copies of state and federal documents that describe program requirements (if these are bulky, and the contract administrator can easily access them, it is probably not necessary for them to have complete copies in their files).
- Budget and budget adjustments;
- A Copy of RFB/RFP and contractor's response;
- A Copy of the contract and any contract amendments;
- Copies of written correspondence and notes from meetings and phone conversations, with dates and action taken;
- Records of progress or routine reports required of contractor;
- Copies of significant financial documentation, such as expense reports and correspondence relating to audits;
- Documentation of any failure to meet performance expectations, along with plan of correction and evidence that corrective action plans have been implemented by the contractor. All documentation should clearly indicate whether proposed actions were agreed upon by both parties, and if follow-up is required; and
- A written record of any changes or interpretations that have been made in regard to the contract (which must be agreed to by Department management).

C. What can the contract administrator do to ensure good communication with the contractor and that the project gets off on the right foot?

Some problems in contract management can be avoided or minimized if minor disputes, conflicts and misunderstandings are recognized and addressed. It is therefore important to make sure everyone involved in the contracted project has a common understanding of roles and expectations. There should be an emphasis on open and constant communication between the contractor and the contract administrator, with consistent setting and enforcement of the Department's expectations under the contract. Misunderstandings at this point can be resolved much more easily than ones cropping up during the life of the contract. Holding a start-up conference is often a useful way to begin a new contract. If it is decided not to hold a conference, the same information needs to be discussed and clarified, and records of these discussions put in writing.

Who should be involved in a start-up conference?

The start-up conference is a review session for those who have been involved in developing and negotiating the contract, but for some in attendance, it may be an introductory session. The complexity of the service and the governing contract will dictate the cast of characters who should be invited to a start-up conference. At a minimum, the contract administrator and contractor's representative need to be present. Since the role of subcontractors needs to be clearly defined, they all should be present, if possible, during the start-up conference.

What information needs to be reviewed with the contractor, whether in a conference or otherwise?

To ensure a common understanding of expectations, all aspects of the contract should be reviewed, including referenced materials. Other topics that should be reviewed at the beginning of the contract are:

- Any questions about contract terms and conditions, as well as contractor prohibitions such as promotional advertising, news releases, disclosure of confidential or proprietary information, etc.;
- Contractual requirements such as insurance, Affirmative Action/Civil Rights Compliance (AA/CRC) plans, lobbying, and prohibitions against tobacco smoke for children's programs, should also be reviewed;
- The project work plan or schedule, along with a discussion of contingencies in the event of any disruptions;
- Procedures for changes in the work plan or other aspects of the contract, as well as procedures for cancellation or termination of the contract; and

- The contract administrator's plan for monitoring contractor performance. This would typically include reporting requirements, a tentative schedule of site visits, and identification of areas where the contractor may need technical assistance, either in programmatic or financial areas. It is the responsibility of the contract administrator to directly provide, or identify other resources for, any needed technical assistance and to assure that it has been provided.

D. What does the contract administrator need to tell the contractor about payment procedures?

There is nothing more important to the contractor than payment procedures. The forms to be used for fiscal reporting and the payment schedule are set in the contract, and a review of these terms is needed.

Because it is necessary for contractors to receive funding to begin the program before they are able to report expenses or bill for services, prepayments are made for many contracts. The contractor should understand that the pre-payment will be reconciled to reported expenditures, and pre-payment amounts that have not been earned will be recovered during the last months of the contract. In other words, the contractor is not necessarily able to keep the entire pre-payment, but needs to submit expense reports or billings sufficient to earn the pre-payment amounts.

The contract administrator should also be sure the contractor understands:

- That all services provided or all allowable costs must be reported, even if they exceed the contract. While payments in excess of the contract limit will not be made, complete information on the number of service units provided or allowable costs expended will put the contractor in a better position to develop future budgets and make other necessary financial decisions; and
- That the contractor is responsible for periodically reconciling reported expenditures and payments with their accounting records. If subsequent audits show they have under-reported or over-reported expenses, they may lose the opportunity to claim funds that were available or, worse, need to pay back unearned funds.

E. What does the contract administrator need to tell the contractor about allowable administrative costs?

An area of particular confusion concerns administrative and support costs charged to the contract. Some agencies have a misconception that if they spend all funds according to the project budget accepted by DHFS, all these expenditures will be allowed. That is not necessarily the case.

DHFS does not require extensive pre-contract analysis to confirm that administrative costs

included in the provider's budget are reasonable, but instead relies on the provider's annual audit to determine the allowability of administrative costs. In other words, just because DHFS accepts the grant budget, this does not mean the Department will accept every expenditure made during the grant period, even if it is consistent with the budget.

For example, a project budget could include an amount the contractor will charge for rental costs, but DHFS does not require the contractor to provide information showing that the budgeted amount is reasonable. If the audit later shows that the DHFS contract paid for 25% of the agency's staff, but for 75% of the rental costs, it could conclude the DHFS contract was overcharged for rent, and disallow some of that cost.

This example clarifies the point that approval of the general program budget does not guarantee allowability of expenses. Contract administrators should remind providers that the allowability of expenditures will be monitored during the contract period and tested by independent auditors, and that the Department will act on any findings.

F. What does the contract administrator need to tell the contractor about subcontracting?

Subcontracting is a particularly important practice for counties and tribes, which may subcontract for most or all of their services. As prime contractor, the county retains responsibility for fulfillment of all terms and conditions of the contract (and contract addenda). Chapter B-7 of the *Financial Management Manual* contains useful information, and a base model contract, for counties and tribes to use.

Standard contract language for grants stipulates that DHFS approval may be required regarding the subcontractor selection process, the providers selected, and the terms and conditions of the subcontracts. Specific procedures the contract administrator will use to give these approvals should be reviewed at this time.

F. Are there any other information resources contractors should know about?

Contractors are required to follow applicable state and federal rules and regulations and it is the contract administrator's responsibility to determine that they do so. Some of the major sources of general information on program requirements include federal and state statutes, state administrative rules, federal regulations, program manuals, administrative memos, and other information referenced in the contract.

In the fiscal area, some of the major sources of information on requirements that must be complied with are found on the DHFS website in the Grants and Purchases section. Contractors who do not have access to that site will need to rely on their DHFS contract administrator to provide them with copies of necessary documents. See Contracting Policies and Procedures for a listing of some documents contractors should know about.

II. Contract Monitoring and Provider Technical Assistance.

A. What is the difference between technical assistance and contract monitoring? What are the specific activities a contract administrator engages in when monitoring contractor performance and providing technical assistance?

Technical assistance and contract monitoring are actually complementary activities; both aimed at ensuring the best results for the target population and other program stakeholders. To ensure optimum performance, the contract administrator must fully manage the contract by both monitoring the program's progress and providing information and technical assistance that will help the contractor achieve the best results.

In general, when monitoring contract performance and providing technical assistance, contract administrators spend time:

- Maintaining the lines of communication, being aware of operational issues in the contractor agency, and helping resolve any problems that might interfere with program success. This will involve staying in contact with the contractor's program managers and staff. This might also require meeting with boards of directors and/or reviewing minutes of board meetings as well as of county human, community or social services board meetings;
- Reviewing written reports submitted by the contractor, to be aware of any programmatic or budgetary problems. At times, it might be useful to review CARS reports, as well;
- Making site visits to observe services being delivered, to review program progress with staff and managers, to review bylaws or policies for compliance with federal requirements, and/or to review overall agency management. The sample monitoring tools in the appendix may be useful to document information collected during site visits;
- Resolving disputes and developing plans of correction. Minor disputes, which might be differences of opinion about contract terms or other program expectations, generally are solved quickly and the services go on. However, questions about the quality of contractor performance generally call for involvement of other Department staff in both the program and fiscal/audit areas; and
- Documenting technical assistance and monitoring activities, including steps taken to resolve disputes. In case of a dispute, documentation will establish the facts and, if necessary, provide the basis for decisions to revise, suspend or terminate the contract. Documentation might also help protect the Department and contract administrator from contractor claims.

The contract administrator should keep in the contract file all correspondence to or from the contractor, minutes, and summaries of meetings or phone calls. These should indicate whether proposed actions were agreed upon by both parties, and if follow-up is required. For a specific problem, the contract administrator should keep a log sheet, which identifies the problem, attempted solutions and the results.

All contract files can be considered public records, and proper discretion is advised when documenting communications with or about contractors.

B. How do we make sure the contractor is carrying out the program requirements and adequately meeting the goals and objectives as set forth in the program description?

In addition to meeting the requirements stated in the contract, contractors must comply with all applicable federal and state laws, rules and regulations. The contract administrator must be well acquainted with these, and ensure the contractor is both aware of and in compliance with them.

Beyond that, the contract administrator needs to be proactive in looking for any signs that the needs of the target population, as reflected in the contract goals, objectives and outcomes, are not being met. If a contractor is not meeting expectations, the contract administrator needs to be assertive in initiating appropriate actions, which may include negative consequences for the contractor.

In order to determine if the contractor is performing adequately, the contract administrator will need to:

- Review the workplan to check that adequate progress is being made in implementing the various steps and achieving the objectives, goals and outcomes of the project. This includes ensuring that reports and other "deliverables" are submitted on schedule and are of acceptable quality. Deliverables could include periodic progress reports, program evaluations, customer evaluations of services, etc.;
- Observe program activities to ensure services are being delivered and to note any areas where improvement might be needed. Review the contractor's documentation, such as publications the project has produced, records of the numbers of clients served, reports on project outcomes, or schedules of project activities;
- Respond to complaints from clients or other stakeholders about a contractor;
- Provide needed or requested information, training and assistance in the specific service area the contract deals with. Respond to provider requests to assist with subcontracting, or contract modifications or waivers; and
- If payment is tied to performance, determine the extent to which the contractor is meeting performance measures, and authorize appropriate payments.

C. What is the goal in monitoring the contractor's fiscal performance? How does the contract administrator meet those goals?

The contract administrator should ensure that funds are being managed efficiently and effectively to accomplish the objectives for which they were provided. This is done by matching money spent against program expectations, to be sure "we are getting our money's worth" from the provider. The contract budget can be used as a monitoring tool here, since it is basically a spending plan against which fiscal and program performance can be measured. If spending patterns are not as expected, this can be an indication that program performance is not as expected, either.

For instance, the contract administrator should compare expenditure reports to the contract budget to determine if overall project spending is what would be expected at the time of the review. Potential problem areas, such as unspent money combined with a waiting list for services, or monthly expense reports that are always exactly one-twelfth of the yearly contract amount, should be noted and explanations sought from the contractor. The CARS unit regularly disseminates reports that identify programs which are underspending their budgets, and these reports can be helpful in identifying programs which may need attention. Depending on the specific program, the contract administrator may determine other measures of fiscal performance are also appropriate.

Is there another reason to monitor fiscal performance?

Yes. Since agencies are required to have effective financial management systems as a condition of receiving Department funds, contract administrators should be alert to any signs that contracted agencies are not meeting acceptable management standards, and may be asked to assist OPRA in assuring that audits called for in the contract are submitted on schedule.

When is it necessary to take a more detailed look at a provider's fiscal performance?

Division policy may address the level of detail expected in monitoring a contractor's fiscal performance. Also, if expectations for program performance are not being met, it may be necessary to seek an explanation by taking a more detailed look at the contractor's financial records. For instance, are program funds being diverted to other purposes, or not spent on the most important program elements? To learn more about how a contractor is managing DHFS funds, a contract administrator can review agency financial records to determine if:

- Project accounting records match with expenses reported for reimbursement;
- Individual line item expenditures are consistent with line item amounts in the budget. If not, why not? Are line item changes within percentages allowed by the contract?
- Personnel, supplies and services, equipment and space costs seem reasonable and are

consistent with the budget;

- The agency has an indirect cost plan and a cost allocation plan, if these plans are approved and by whom and if they are being followed. Agency policies and practices in this area will be more thoroughly scrutinized during the agency audit, but contract administrators should notice if either the system for allocating costs, or the resultant charges to this contract, do not seem reasonable. (See "reasonable" administrative costs);
- There is adequate documentation of subcontractors' costs;
- Requirements for program "match" funds are being met. This is a matter of the reviewer asking, "How are you meeting match requirements?", and then determining, based on the requirements, if the method is appropriate;
- There are any accounts payable problems, such as delinquent taxes, unpaid bills, or garnishments or liens against the contractor; and
- Any necessary corrective actions based on audit recommendations have been implemented.

What are some fiscal areas in which providers may need technical assistance?

Contract administrators may be called upon to:

- Review and respond to requests for waivers from audit requirements; and
- Respond to provider requests to assist with subcontracting, or contract modifications or waivers. Contract administrators need to involve appropriate DHFS program and fiscal staff in contracting issues, as well.

D. What does the contractor need to do to assure compliance with affirmative action and civil rights requirements?

The Department has the responsibility for determining whether contractors are complying with federal and state laws and regulations for equal opportunity in employment and service delivery. The specific obligations of the provider are described in the model contracts.

As of the publication date of the first version of this manual, the Department's Office of Affirmative Action and Civil Rights Compliance (AA/CRC Office) is working on devising a new system for monitoring contractor compliance with affirmative action and civil rights laws, regulations, and contract provisions. Once this newly devised system is in place, the specific roles that contract administrators are to play in monitoring affirmative action and civil rights compliance will be clarified and communicated to all contract administrators. This information will be integrated into the next version of the *Contract Administrator's Manual*.

In the meantime, contract administrators should be doing the following:

- During on-site visits or through other contacts, determine whether a contractor has any questions or concerns about AA/CRC policies and requirements. If questions

arise, the contract administrator should seek the assistance of the AA/CRC Office in providing answers.

- Pay attention to whether the demographic make-up (i.e. race, gender, age, etc.) of clients served by the contractor appears to reasonably relate to contractual service goals and the overall profile of the target population. If significant differences exist, the contract administrator should seek answers from the contractor and, if necessary, involve the AA/CRC Office.
- Promptly seek the assistance of the AA/CRC Office in handling any complaints of discriminatory action on the part of a contractor that the contract administrator is responsible for monitoring. Because of the sensitive nature and complex legal issues involved, it is important for the Department's AA/CRC Office to be aware of any complaints, and to determine what the Department's response or follow-up should be.
- Be involved, as needed and directed, as a team member in reviews or investigations conducted of allegations of non-compliance by a contractor with AA/CRC policies. The AA/CRC Office will typically take the lead in these reviews, but the contract administrator can be a valuable resource and productive team member in completing needed review work.

In conclusion, the contract administrator is a vital part of the Department's overall effort to monitor contractor compliance with affirmative action and civil rights laws and regulations. Further direction and guidance in this area will be forthcoming. As a general rule, if a contract administrator has any questions about AA/CRC issues, they should feel free to contact the AA/CRC Office.

E. What if there is a problem with program or fiscal accountability?

If there is a problem with accountability, the contract administrator must work with the contractor and other stakeholders to develop any needed plans of correction. For concerns about accomplishment of program outcomes, this might mean revising work plans, either to improve them or respond to changes, providing technical guidance about best practice standards, or increasing monitoring activities. In the fiscal area, corrective action plans might include amending the budget or improving certain management procedures.

What other steps can be taken to deal with contractors that are not meeting expectations?

What action the Department takes with contractors that are not meeting expectations depends on the nature, severity and duration of the problems. Besides requiring the contractor to submit a plan of correction to address the problem, other options available to the Department include:

- Requiring the provider to submit more detailed information about the scope and impact of the problems;

- Intensifying contract monitoring activities by requiring additional reports or by increasing on-site review, perhaps with the assistance of staff from OPRA or elsewhere in the Department;
- Requiring the contractor to supplement CARS forms with additional information, as a condition of receiving payment;
- Withholding approval to proceed to the next phase or to expend certain funds until desired improvements occur;
- Withholding payment entirely until certain information is received or improvement in services occurs;
- Devising a joint strategy with other funders of the provider, which is likely to be more successful than if the Department acts alone;
- Amending the contract to, for example,
 - Allow for payment on a reimbursement basis only, with no prepayments;
 - Require the contractor to obtain technical or management assistance,
 - Require improvements in internal management practices and fiscal controls;
- Having OPRA auditors review problem areas in subsequent audit periods;
- Shifting a portion of contract funds to other providers that are performing well;
- Not renewing the contract, or renewing it for a period less than one year, with further renewals contingent upon making certain improvements; and
- Canceling the contract.

Who decides what enforcement action the Department should take?

Division and bureau program managers should be kept informed of any significant problems a contractor is having, and be involved in formulating the Department's response. At times, BFS, OPRA, OLC and the Secretary's Office will also need to be involved. The contract administrator should keep the provider informed of any potential sanctions for non-performance. If a contractor is having severe problems, immediate action by the Department may be needed.

II. Contract Renewals and Close Outs.

A. When are contracts renewed?

DHFS contracts are generally renewed every year, whether or not purchasing or granting

authority still exists. Typically, the purchasing or granting authority has been given for

the first contract year, plus two one-year renewals, though up to four one-year renewals has been allowed.

Another type of contract renewal occurs when granting or purchasing authority has expired, but it makes sense to continue contracting with the same provider(s) without going through a new competitive RFP or RFB process. In this case, a new request for purchasing or granting authority is prepared by the contract administrator, sometimes with the help of others in the program bureau. Just as with totally new contracts, this request is shepherded through the approval process by the Purchases and Services Section in BFS.

Is it possible to carry over unspent money from one contract year to the next?

Carrying over unspent funds from one year to the next is usually not allowed. Any request to do so must be reviewed for compliance with federal and state appropriation language, and appropriate approval obtained through the pre-contract packet review process. If federal funds are involved, it may also be necessary to obtain federal approval to carry over funding into the next contract period.

When is a new RFP or RFB required? Who makes that decision?

Competitive procurement processes provide a level playing field for possible contractors, and may result in better prices and higher quality of services. For these reasons, Department policy is to go through a new vendor selection, such as a RFP/RFB, unless there are convincing reasons not to do so.

In deciding whether a new RFP or RFB should be issued, the following factors could be considered:

- Whether the nature of the program, and work required by provider(s), is expected to change significantly;
- The extent to which the work is ongoing and requires continuity from the same provider(s);
- The amount of resources provider(s) invested in order to start the program;
- Changes in the provider community, such as new agencies expressing interest in competing for the contract; or
- Poor performance by current provider(s).
- When requesting new granting or purchasing authority, bureau program staff make a recommendation either to renew contracts with the same providers, or to issue a new RFP/RFB. This is reviewed by BFS Purchases and Services staff, who forward a recommendation to the Deputy Secretary.

How much time is required for a contract renewal?

The contract renewal process needs to begin early enough to ensure the provider(s) first payments are made on time and services to clients are not interrupted. Exactly how long this will take depends on whether a new RGA/RPA is required, and how long it will require the program bureau and provider to negotiate any changes. New contract administrators should seek guidance from division or bureau policies and practices about specific details of the contract renewal process in their program area.

If a new RFP/RFB is issued, the entire process will take considerably longer before new contracts are in place. Refer to the section on "Vendor Selection" and "Contract Processing," for a detailed discussion of this process.

B. What is the contract administrator's responsibilities in the contract renewal process?

As the point person in renewing the contract, the contract administrator must:

- Determine whether to continue the contract with the provider(s). This decision will be based on information gathered from monitoring and technical assistance activities, and be dependent upon satisfactory progress toward meeting program goals and objectives, and over-all program management. If a site visit will be scheduled before determining whether to renew the contract, keep in mind the timelines required for pre-contract packet approval and contract signing;
- Determine the level of funding available for the provider(s) for the next year. There may have been changes in the amount of money available to the Department, or it may have been decided to decrease funding to a particular provider because of poor performance;
- Notify providers about the renewal process. Providers typically submit applications, with proposed budgets and workplans, for each new funding year. Before they can do this, the contract administrator must notify them what level of funding will be available, when applications must be received, and what information should be included;
- Negotiate any changes to the contract. This could include changes in the workplan, as well as the budget. If any management problems have been identified during the past contract year, additional requirements may be added to the contract. Also, after the contractor has a history with the Department, past audits may indicate performance problems that need to be considered when negotiating contract renewals. The contractor may need technical assistance in complying with any new contract terms, including revised workplans;
- Shepherd documents through the approval process. If purchasing or granting authority has expired, an RGA or RPA (see RPA/RGA) must be prepared, this request is

shepherded through the approval process by the Purchases and Services Section in BFS. For every contract renewal, a new pre-contract packet must be prepared and submitted to BFS, which gives fiscal approval to contract; and

- Prepare the contract, including model contract language and exhibits. The contract must be signed by the provider and division administrator, and sent to CARS in time to ensure the first payment goes to the provider on time.

Since specific contract renewal practices vary across the Department, contract administrators must be knowledgeable of the policies and procedures in their own program areas. Although some program areas are streamlining this process, it is important to allow sufficient time for all necessary steps. Follow the time guidelines in the Accounting Policies and Procedures Manual, Contract Administration Policy 1.0.

B. What does it mean to "close out" a contract, and how does this happen?

Final program reports on the extent to which desired outcomes have been accomplished should be received within the timeframe stipulated in the contract.

Final expenditure reports should be received within 90 days after the end of the contract period, unless a different (usually earlier) time has been specified in the contract. The contract is then closed by reconciling reported expenditures to payments made, and paying out or recovering any moneys due to or from the provider. If money is due the Department, it is generally collected by reducing future payments to the provider. In certain situations, such as after the first year of a two-year grant, or if a discretionary federal grant is extended, unspent funds may be carried over into the next year.

The deadline for filing the final expenditure report may be extended by the contract administrator, but these requests should be discussed with BFS before approval is given. All requests and responses should be in writing, and copies of approval or disapproval of the request should also be sent to the CARS unit.

IV. Audits.

A. Auditing Basics.

Why are audits required?

Audits are required for many reasons. They may be required by state and/or federal law. In addition, audits are one important means by which the Department obtains an independent assurance that a provider agency complied with department fiscal policies. Good business practice and the need to satisfy federal requirements that DHFS is monitoring federal funds administered by the Department, have contributed to the Department's requirement that annual independent audits need to be submitted by provider agencies unless waived by the

Department.

Besides fulfilling a state statutory and/or federal law requirement, audits can actually accomplish important monitoring objectives. Some of the key things audits can tell the Department are whether a contractor:

- Is in good financial condition, since poor or deteriorating financial condition could jeopardize a contractor's ability to fulfill contract obligations;
- Has complied with applicable accounting and audit guidelines;
- Has appropriately spent or returned all funds according to the terms of the contract; and
- Has in place effective internal fiscal controls, which enhances its ability to safely manage Department funds.

Are audits always required?

Language in the model contract requires a provider organization to submit an annual independent audit whenever it receives more than \$25,000 in DHFS funds during its fiscal year. The funds can be provided either directly by DHFS, or by a pass-through agency, such as a county. The Department is currently seeking a statutory change to raise the threshold to \$50,000, in an effort to moderate audit costs and keep pace with federal audit policy changes.

Requests for waivers of the audit requirement may come first to the contract administrator, and should be evaluated by managers in the appropriate program division(s) and OPRA against the following criteria:

- If the cost of an audit exceeds 5% of the total contract, an alternate years audit schedule that covers both years may be approved;
- For larger organizations, for which the Department business constitutes only a small part of the total operation, a corporate certified audit report along with a statement of revenues and expenses for the contracted services may be accepted in lieu of an audit of the contracted services; and
- If it is determined that an audit would not be cost effective, or would otherwise place an undue burden upon the vendor, the audit requirement may be waived. The specific circumstances, which support the granting of a waiver, must be fully documented by Department staff, and an alternate form of financial monitoring must be substituted. This could mean additional reviews of program spending, site visits, etc.

When are audits done? Are they timely enough to help monitor current contracts?

Certified annual audits of non-governmental organizations are received by the Department within 180 days of the close of the agency fiscal year. They are thus not useful measures of current contractor performance, but they do give an indication of over-all fiscal responsibility. If an audit

found significant problems in a past contract, the contract administrator will want to ensure adequate safeguards are in place so the same or similar problems do not recur.

How do provider agencies pay for audits that occur after the contract period has ended?

Audit expenses are allowable if the audit is required by federal or state law or regulation, or is authorized by the Department, and if it is performed in accordance with applicable federal and state guidelines. Providers typically build the current year's audit expense into their budgets, even though that audit looks at the prior year's expenditures.

B. Contract Administrators' Role in the Audit Process.

What can the contract administrator rely on OPRA to do regarding audits?

OPRA takes the lead in working with program divisions to confirm which agencies owe DHFS audit reports. Once this is confirmed, OPRA is responsible for:

- Obtaining the audit reports and reviewing them to confirm that they comply with Department standards;
- Determining if there are audit issues which involve DHFS funds;
- Working with the contract administrator to resolve any significant audit issues, such as where a provider agency misspent grant funds and violated the Department's Allowable Cost Policy Manual; and
- Closing out audit reports once all audit issues are settled.

How can contract administrators use audits for monitoring purposes?

Under certain circumstances, it may be appropriate for the contract administrator to rely on the annual audits to obtain needed monitoring information. In response to a major policy change related to a federal grant, for example, OPRA and the contract administrator can develop new audit policy and instructions that ensure the annual audit will obtain information necessary to determine if the contractor is in compliance with the new requirements.

What should the contract administrator do if he/she discovers something that could be an audit issue?

Any knowledge or suspicion of activities that might cause concern in a future audit should be dealt with immediately by the contract administrator. This might include increased monitoring or technical assistance by the contract administrator. Bureau and division staff should be informed of the situation and involved in deciding how to resolve the issue. It may be decided to involve

OLC and OPRA as well.

What work related to reviewing and resolving audits is the responsibility of the contract administrator?

The involvement of the contract administrator in the audit review and resolution process can vary widely. If the contract administrator has been dealing with any problem agencies, he/she should alert OPRA, so the audits of these agencies receive prompt, thorough attention. In many instances, audits are easily obtained and determined to be "clean" (i.e., no issues to address), and the contract administrator will have no involvement in the audit process. However, for other audits, the contract administrator may be called upon to do some of the following:

- Help obtain an audit from an agency which isn't responding to inquiries from OPRA;
- Coordinate development of the program division's response to problems identified by a contractor's audit, such as determining the amount of grant funds to be returned to the Department, or the best strategy to promote improved financial management practices by the provider agency;
- Participate in a site visit to assess the implementation and effectiveness of an agency's corrective action plan; and
- Work with OPRA in devising special contract language to address recurring audit and financial management problems exhibited by an agency.

If recoupment of audit disallowances is necessary, how does this work and what does the contract administrator need to do?

The contract administrator, along with audit, fiscal and legal staff, determines the appropriate approach to take in recovering funds from the contractor. Options include:

- If provider has another contract in effect, BFS can reduce subsequent payments;
- The agency can be sent an invoice. Under this procedure, OPRA sends two letters to the agency requesting payment. If the agency does not pay, OPRA refers the collection to BFS, which follows the procedures in the Department Accounting Policies and Procedures manual; and
- High-risk vendors are handled in ways appropriate to the circumstances and determined by division, OPRA, OLC, and the Secretary's office.

V. Ethical Standards for Contract Administrators.

Are there any special standards of conduct for contract administrators? Where are they found?

All Department employees are expected to avoid any conflicts of interest, but in the context of contract administration, these standards take on even broader scope and definition. Contract administrators must make every effort to avoid even the appearance of reaping financial benefit or any other personal advantage for themselves, their immediate families, or organizations with which they are associated. This includes accepting anything that could reasonably be expected to influence their actions or judgment, or could reasonably be considered as a reward for any action or inaction on their part.

"Reasonableness" is open to interpretation by any observer. These observers could include other vendors, taxpayers, the media, legislators, peers, employees or management. What one person might consider acceptable may be unacceptable to someone else. Therefore, the only standard to adhere to is to avoid even the perception of accepting something of value from a contract agency.

What should a contract administrator do if a contractor provides coffee, rolls and lunches?

As with gifts and promotional items, contract administrators need to maintain the appearance of objectivity in situations where contractors provide food and beverages. However, some judgment is needed in this area. Accepting a cup of coffee or eating a lunch provided to everyone at a meeting or conference, for instance, would be perceived differently than accepting an expensive lunch at a restaurant. DHFS contract administrators should pay their own way when eating out with contractors or other providers who are potential contractors.

What about accepting gifts or promotional materials from providers?

Gifts or promotional items from vendors, providers or grantees also are problematic. If an advertising promotion gift, such as a coffee mug, comes to a contract administrator through his or her position, it should not be accepted. Acceptance could be perceived as an endorsement of a particular product or service. Similarly, accepting a gift from a provider could be seen as compromising the objectivity of the contract administrator, who has an enforcement role. Vendors are usually very understanding, appreciate being informed of the policy, and will respect the integrity of contract administrators who adhere to it.

What if a contractor asks for a testimonial or reference?

Contract administrators should be guided by state policy that prohibits state purchasing officers from issuing letters of endorsement and/or testimonials for any materials, supplies, equipment or services. By extension, this applies to contract administrators and anyone involved in the contractual relationship with a provider. Contract administrators also have a responsibility to

monitor vendor promotional materials for violations of the policy prohibiting advertising related to state contracts.

These prohibitions, however, do not extend to references. When asked, contract administrators may respond to straightforward reference checks with statements regarding the contractual relationship and whether performance was satisfactory or not.

Is it appropriate to socialize with contractors?

Contract administrators must not do anything that may give the appearance of favoritism to one provider over another, and social interaction with providers should be considered carefully. Even if a contract administrator is paying his/her own way, the propriety of being seen in a social setting with a vendor may be questioned. Others may perceive the situation differently. Ask yourself: How will it look in the newspapers? To another vendor? To anyone?

A DHFS staff person assigned as a contract administrator may also have other professional contacts with provider staff in non-contract situations. These situations need not be problematic as long as the contract administrator uses good professional judgment and avoids doing anything that could reasonably be construed as favoritism. A good rule of thumb is "Don't allow yourself to be caught in any situation with a contractor that you wouldn't want to read about in the morning paper."

What if a contract administrator has another job, and comes into contact with a provider there?

Outside employment, which may pose a conflict of interest, must be reviewed and approved prior to acceptance of the employment. Approval must be sought through the Department's supervisory chain of command. In general, the standard of conduct calls for written disclosure of the nature and extent of the relationship or interest prior to contracting.

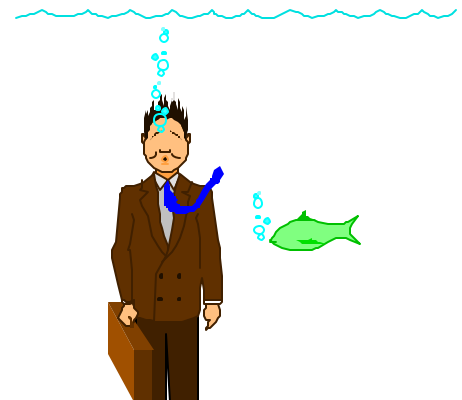
11 Words of wisdom from contract administrators

As part of the Office of Program Review and Audit's on-going efforts to develop a contract administration course for DHFS contract administrators (we're still working on it!), we surveyed many contract administrators – from the most experienced to some of the more recent rookies – to identify training needs. We learned a lot through these surveys. Two items that we learned we want to share with you.

First, we collected a lot of valuable insights from staff on the indicators they rely upon to tell them when a provider they are overseeing may be experiencing problems. These observations are summarized below. On the next page, we offer some helpful hints and ideas from experienced staff on the things they learned to do over the years to better ensure that their contracts ran smoothly.

RED FLAGS - otherwise known as **BETTER LOOK INTO IT!**

- 📁 Recurring staff changes and turnover
- 📁 Poor leadership in the agency
- 📁 Services are not occurring as proposed and approved
- 📁 You're not receiving expenditure reports
- 📁 You're not receiving progress reports.
- 📁 Levels of expenditure are not as proposed and approved (over and underspending)
- 📁 Continually changing budget lines
- 📁 Vague responses to your questions from agency staff
- 📁 You hear reports from the community and/or clients regarding concerns/problems with an agency
- 📁 The agency's application, goals, objectives, etc. are of poor quality
- 📁 The Provider doesn't have updated practices or program information
- 📁 Communication is lessening – find out why
- 📁 Workplans are not being followed
- 📁 The program doesn't have controls or QA in place - unaware of their own performance
- 📁 Problems in a seemingly unrelated area may indicate problems in contract areas



What indicators do you and your peers use?

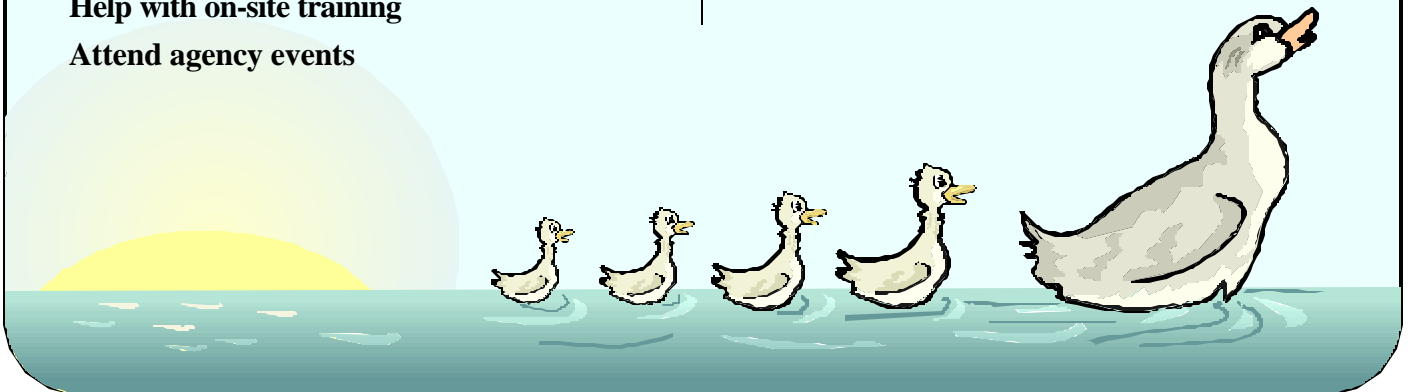
Helpful Practices For Effective Contract Administration

Establish Good Working Relationships With Agencies

- Be responsive**
- Meet regularly**
- Be a resource for the agency**
- Organize meetings for grantees**
- Provide updated information**
- Encourage them to expand funding sources**
- Provide feedback**
- Polish your public relations skills**
- Use networking**
- Help with on-site training**
- Attend agency events**

Get And Stay Organized

- Plan ahead**
- Use a database**
- Maintain a contact list**
- Develop and/or use a checklist**
- Develop and use tickler files**
- Know where to go for information**
- Keep your supervisor updated**
- Don't be afraid to try something different**
- Always be aware of the bigger picture**



12 Action steps

It is one thing to collect and review information during the monitoring phase of the overall contracting process. It's another thing to put it to use. A whole host of options exist on how to react to evidence of provider performance problems, and a number of considerations need to be made in making the choice.

In order to clarify the purchaser's options for action, the Office of Program Review and Audit a while back put together the following list of alternative action steps that a purchaser could consider when responding to inadequate performance by a provider under contract. The list of options is presented generally in order from least to most severe actions that could be taken. There are a few key points we would emphasize in using this list.

- ⇒ There is no one course of action that is always correct in every situation. The best course of action is the one that best fits the unique circumstances the purchaser is facing.
- ⇒ The number of options is not limited to the length of the list offered below. Purchasers should be creative and strive to devise the best solution that meets the purchaser's needs.
- ⇒ Whatever action is taken, the point is...take action, and do so in a timely manner. The purchaser's monitoring efforts, and the overall effectiveness of the purchaser's contracting function, will be eroded if the purchaser fails to act on evidence that a provider's performance is below expectations.
- ⇒ The initial course of action chosen by the purchaser should be proportionate and be considered as part of a larger strategy that could lead to progressively more serious actions of the provider is not responsive and performance deteriorates.

The Department will take whatever steps the Department deems necessary to protect the State's interest and promote achievement of program and contract objectives and requirements. The range of action steps the Department can and will consider using is wide ranging and includes, but is not limited to, the following:

1. **Technical Assistance.** Department staff may provide hands-on assistance in showing provider staff how to address a problem through changes in policies or procedures, or through some other action.

2. ***Improvement or Corrective Action Plan.*** The Department may require a provider to develop a plan of improvement which describes the specific action steps the provider will take to address one or more performance or compliance concerns.
3. ***Collaborative Exploration of Issues.*** The Department may offer to work collaboratively with the provider to identify solutions to a program problem that neither side anticipated, can readily identify the causes of, can confidently propose solutions to.
4. ***Clarify/Reinforce Expectations.*** In circumstances in which the Department chooses to acknowledge a provider's claim that departmental expectations are not entirely clear, the Department may act to more specifically clarify expectations of the provider, including a clarifying statement of the consequences of failing to meet expectations.
5. ***Training.*** The Department may require more formal, systematic training of appropriate provider staff, if it is believed that targeted technical assistance is not likely to be sufficient to address the performance issues.
6. ***Enhanced Monitoring.*** The Department may have monitoring staff engage in more frequent, in-depth, and wider ranging monitoring activities, in order to determine the scope and causes of performance concerns, and to independently confirm that progress in making improvements is being made.
7. ***Increased Reporting.*** The Department may require a provider to change the type or amount of information submitted, or increase the frequency of reporting, as part of an enhanced effort to confirm that performance is improving.
8. ***Amend the Contract.*** The Department may seek an amendment to the contract to include changed policies, provider obligations, payment provisions, and/or reporting requirements, in order to enhance the Department's leverage in ensuring that improvements are made.
9. ***Withhold Payment.*** The Department may withhold all or a portion of a contract payment until one or more specified actions have been fully implemented by the provider.
10. ***Invoke a penalty.*** The Department may invoke a non-refundable penalty against a provider for failing to meet a particularly important contract or program requirement.
11. ***Reduce the Contract Amount.*** The Department may reduce the amount to be paid under the contract with a provider, and shift funding to other providers, if the option exists to take this action. This action would promote improved overall performance of the system and reduce the Department's risk of doing business with a provider which is experiencing persistent, material performance problems.
12. ***Non-renewal or Cancel the Contract.*** The Department may choose either to not renew

the contract with a provider and seek a new agency to contract with, or to exercise its option to cancel a contract, rather than wait for contract renewal time.

When presented with evidence of a performance gap, the Department is committed to choosing a course of action that is reasoned, proportionate, and most likely to protect the State's interest while promoting improved performance. In deciding on a course of action to take, it is a good idea to weigh and consider a number of factors, including:

- ***Frequency.*** Isolated instances on non-compliance will be viewed as less serious than numerous, documented instances of non-compliance with the same program requirement.
- ***Breadth.*** Instances of non-compliance with single a requirement, such as inconsistent documentation of client contacts, will be viewed as less serious than a circumstance where non-compliance with this requirement is accompanied with a wider array of other types of non-compliance or performance concerns.
- ***Magnitude.*** Non-compliance with, for example, a timeliness requirement will be viewed as less serious when achievement of the timeliness standard is routinely missed by perhaps 3 to 5 percent, as compared with a larger magnitude of non-compliance, such as 30 to 50 percent.
- ***Severity.*** A performance problem by a provider which, for example, directly contributed to one or more clients facing a material and unacceptable increased risk of being unsafe, will typically be viewed as more serious than non-compliance with requirements that are more administrative in nature.
- ***Pattern.*** A first-time failure by a provider to meet a requirement, especially after a pattern of sound performance had been established, will generally be viewed as less serious than a provider which has persistently failed to meet a standard, especially if the magnitude of poor performance is worsening.
- ***Provider Effort.*** A provider which fails to meet a standard, yet demonstrates a concerted effort to implement corrective actions and a willingness to take new improvement efforts, may face a different set of department actions than a provider which fails to cooperate and take reasonable action.

13 Canceling or non-renewing contracts

On selected occasions, the Office of Program Review and Audit has consulted and worked with program division on how to handle the prospects of canceling a contract with a provider that was not performing. In order to organize our thinking to ensure that the case was made for cancellation of the contract – as opposed to a host of the other options available to the department – we created the document on the following pages.

This document describes a “best case” scenario of the things a purchaser should strive to do or consider at the various stages of the contract in order to make a reasonable case to cancel a contract. We would like to emphasize that by no means is this document intended to assert that all of the items below must have been done, or that these are standards rooted in contract law. In fact, most purchasers, like DHFS, have a contract provision authorizing either party to cancel the contract, for whatever reason, with reasonable advance notice (30 days in our provider contracts). So, technically none of the items below need to be done to legally cancel a contract.

However, our department, probably not unlike most other purchasers, wants our providers to succeed. We want to work with our providers to maximize their chance of accomplishing contract objectives, all the while recognizing that the providers ultimately are responsible for fulfilling their contractual obligations. And, if we face the difficult decision to cancel a contract, we want to know that we have been fair and did what we could to promote success. We also face the practical reality of certain forces probably objecting to any contract cancellation or non-renewal decision. We need to be able to show that, on the one hand, we did our part to assist the provider in being successful, but on the other, we must act to find another provider if we are to achieve larger program objectives. The list of “things to do/think about” is intended to put a purchaser in a better position to make a reasonable, defensible position to cancel or non-renew a contract, if such a decision must be made.

The document on the following pages is in two parts. The first is the shorter, straight-forward list of things the purchaser should do in order to build the case to cancel or non-renew a contract. The second two pages re-creates this list, but includes inserts (as italicized quotes) capturing what we’ve observed as common complaints providers might offer to hearing that their contract might be cancelled. The way we view it, if the purchaser took the right actions throughout the course of the contract, the purchaser will be in a good position to respond effectively to these complaints.

Canceling Or Non-Renewing Contracts

If we want to make certain a decision to cancel or non-renew a contract is sustained, we need to be sure that:

1. Standards of performance are realistic, clearly communicated in the contract, and consistently reinforced through subsequent communications.
2. A written monitoring plan is developed that describes a systematic, fair, and timely process for collecting and analyzing information about the extent to which the contractee is meeting contractual performance standards.
3. The monitoring plan for a contractee is generally consistent with plans for other agencies. Variances are readily explained based on a reasonable, documented assessment of the need to treat providers differently. For example, a more extensive monitoring plan is needed for providers exhibiting serious performance problems.
4. The steps taken to implement the monitoring plan are fully documented, which would include documenting information collection activities, analyses, monitoring results, and follow-up.
5. Analysis of monitoring information is objective, thorough, and results in a written communication to the contractee about areas of performance that do not meet standards.
6. All communications about performance problems based on monitoring activities are timely, specific, and include reasonable and clear timelines for improving performance and consequences if performance is not improved.
7. Any communication from the contractee, which states concerns or offers additional information, is responded to in a prompt, professional manner that focuses on the primary goal of objectively determining whether the contractee is meeting expectations.
8. The consequences for non-performance are reasonable, proportionate, and consistently applied to all contractees.
9. The overall tone of the monitoring and contract enforcement process is objective, balanced, and professional. The attitude and demeanor is exhibited is that the department wants all contractees to succeed and does what it can to promote success, but ultimately the contractee is responsible for meeting performance standards and must be held to account.

The following is the same as above, but includes more on why we need to have a carefully crafted contract phase-out process. Following each standard is an italicized quotes, which reflect complaints or statements from contractees that we might hear in response to efforts to cancel or non-renew a contract.

1. Standards of performance are realistic, clearly communicated in the contract, and consistently reinforced through subsequent communications.

"You never told me what the requirements were, so how can you say that I'm not performing to your expectations? Besides, your standards are not realistic. We were never given enough time or resources to meet these standards, and we aren't even convinced that meeting these standards are necessary to give clients the quality level of services that they need."

2. A written monitoring plan is developed that describes a systematic, fair, and timely process for collecting and analyzing information about the extent to which the contractee is meeting contractual performance standards.

"Your monitoring approach was aimless, haphazard, and burdensome on us. We couldn't figure out what information you wanted, or why. The process got in the way of us doing what we were contracted to do."

3. The monitoring plan for a contractee is generally consistent with plans for other agencies. Variances are readily explained based on a reasonable, documented assessment of the need to treat providers differently. For example, a more extensive monitoring plan is needed for providers exhibiting serious performance problems.

"You were being unfair to us and picking on us. No one else was scrutinized to the extent that we were, and no one else had to meet the standards that we did."

4. The steps taken to implement the monitoring plan are fully documented, which would include documenting information collection activities, analyses, overall conclusions, and follow-up.

"You can't even document how you monitored our performance. How can we be confident that your approach was fair and your conclusions are justified?"

5. Analysis of monitoring information is objective, thorough, and results in a written communication to the contractee about areas of performance that do not meet standards.

"Your analysis is weak, faulty, and clearly shows a bias against our agency. You never provided us with a written explanation of what we were doing wrong. How could we improve?"

6. All communications about performance problems based on monitoring activities are timely, specific, and include reasonable timelines for improving performance and consequences if performance is not improved.

"Your reports about how we were doing were always vague and never on time. It never was clear what would happen if these "vague" improvements were not made. When we finally did get a clearer sense of what you wanted, we didn't have enough time to make changes."

7. Any communication from the contractee, which states concerns or offers additional information, is responded to in a prompt, professional manner that focuses on the primary goal of objectively determining whether the contractee is meeting expectations.

"When we shared information with you about what we were doing, we never got a clear statement about whether or not we were on the right track."

8. The consequences for non-performance are reasonable, proportionate, and consistently applied to all contractees.

"You are overreaching. Sure, maybe we need to make improvements, and we have, but you are taking an action that is out of line and will harm the clients. You haven't done this to other contractees that are having similar problems."

9. The overall tone of the monitoring and contract enforcement process is objective, balanced, and professional. The attitude and demeanor exhibited is that the department wants all contractees to succeed and does what it can to promote success, but ultimately the contractee is responsible for meeting performance standards and must be held to account.

"You weren't helpful in assisting us in truly making improvements. All we ever got was statements about what was wrong. It seemed your staff were seeking out any problem they could find - big or small - just for the sake of doing so. They never seemed to want to hear our side, or to focus on what's good and how things can get better."